EVERYONE'S GUIDE TO FINANCIAL PLANNING

By Helen P. Rogers

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Everyone's Guide To Financial Planning

WINN: When, If Not Now?

Preface

I took liberties with the last line of a famous quotation attributed to Hillel (60 B.C. - A.D. 10) and used it for the title of this book:

"When, If Not Now?"

The entire quotation reads: *"If I am not for myself then who is for me?*
If I am only for myself what good am I?
If not now, when?"

The second line gave me the motivation necessary to write this book. The third line is meant to give *you* motivation to do something about your life.

Many people feel they cannot afford professional advice when it comes to planning for their productive and financial future. In reality they cannot afford to be without this advice!

What can advice do for me? How much will it cost (or benefit me in terms of savings)? How do I choose an advisor? The answers to these and other questions are found in this book.

This is as close as one can get to a "do it yourself" book in a field that does not easily lend itself to the self-help concept. The purpose of this book is to educate you to the fact that you can benefit from professional advice and to show you that such advice should *save* rather than *cost* you in terms of time and dollars.

However, it is up to you to choose your advisers wisely and to monitor their counsel. Rare is the person who has not suffered at one time or another at the hands of an incompetent professional whether he be plumber, mechanic, investment adviser or doctor. The incompetence of an attorney dramatically changed ten years of my life -- in response I studied law. I don't suggest you pursue surgery as a career if you have been the victim of an unnecessary operation, but study you must. Gather information and compare opinions before making the decisions that are ultimately yours alone to make. To purchase stock solely on the recommendation of your broker is foolish. Listen, get other opinions and check out the recommended company. This book and others will tell you the many things you must take into consideration before choosing the insurance, savings, investment, retirement and estate plant hat is best for you. Remember, advice in the area of financial planning must always be taken as a whole, not piecemeal, and in the light of your unique circumstances.

The purpose of this book is to educate not indoctrinate. The only point of view I wish to advocate is the need for critical analysis. No one has your interests more at heart than you do! No one knows your situation, your hopes, desires and needs as well as you. In the long run you and no one else is responsible for the satisfaction or disappointments you get out of life. You can

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respond to events haphazardly as they work on you or you can, through advanced planning, anticipate and control events rather than always being controlled by them.

Isn't it time you took charge of your life? *W I N N*

WHEN, IF NOT NOW?

Section One
Self Analysis

W I N N
When, If Not Now?

Planning is one of those things everyone knows he should do but usually puts off until a more opportune time. Living without a plan is like drifting in a boat. You may, with the proper attitude, have a marvelous time and even eventually reach the destination you had in the back of your mind all the time, but that happens only rarely. Shakespeare put it this way: "Fortune brings in some boats that are not steered." More often the drifter encounters storms for which he is not adequately prepared and may crack up on unseen rocks. Even if he manages to survive he may find he has had to put in at a port far different than the one he would have chosen. Even the lucky ones who seem to do all right without charts and maps to guide them, could have reached their destination and gone on to even more fascinating places with a little planning and discipline.

A lot has been said lately about financial planning; a relatively fledgling profession in its own right. Much of what the new financial planner does was formerly the exclusive province of the insurance salesman, the investment adviser and estate planning attorney. Unfortunately "estate" is a word which conjures up images in most people's minds either of the holdings of millionaires -- especially groomed gardens and iron gates -- or is associated with death. Financial planning brings to mind counsel for the person with money; so much that he needs help in deciding where it should be placed. The average man lets his creditors dictate where his money should go. So much to the landlord or mortgage, so much for groceries, clothing, doctors, etc. He has no need for planning for surplus. He is exactly the person who can benefit most from financial planning! I find it unfortunate that this profession has come to be known as estate and financial planning because that title tends to scare away the people who most need such services. Perhaps it should be designated the "Goal implementation" profession; the art of helping a person establish and achieve his goals in life. Whatever your present position and age you can set and accomplish your goals with proper planning and discipline.

The fact that you are reading this book shows you have decided to stop procrastinating, delaying, and have answered Hillel's ancient question, "If not now, when?" with "NOW!"

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This book will do different things for each reader but I guarantee it will be worth far more to you than the price you paid. If you faithfully pursue the worksheets provided at the end of each chapter you will have a better understanding of your present position in terms of what you really want out of life; what assets you have to work with and information from which to evaluate your strength and weaknesses. Most of you will need professional help in more than one area in forming a plan to get from your present position to where you hope to be. If you have filled in the forms, given careful consideration to the questions and diligently gathered the information required, the cost of professional services (attorney, financial planner, accountant, etc.) should be considerably reduced. You will have anticipated the professional's need to gather data and thereby made the job easier for him and less expensive for yourself.

A minority of you may want to invest the time required to implement a plan on your own. The books recommended at the end of each chapter are for you. However, even though it may sound like a "cop=out", if your assets are vast and goals complicated I would agree with colleagues that you should definitely obtain professional counsel. On the other hand, I have stressed throughout this book that it is the person with the small estate who can benefit most from professional help. The fewer assets the more important each becomes. There is no room for waste due to unfamiliarity with tax codes, investment procedures or trust provisions. Trying to handle your financial and estate planning totally on your own is a perfect example of being "penny wise and pound foolish!" It's just not that easy!

But wait! Don't throw this book away and rush out to the nearest attorney, accountant, or financial planner. It's not that easy either!! In fact what prompted me to write this book is the fact that so many people seem to be extremely docile with their lives and savings. Talk shows on radio and television, magazines, newspapers, seminars, advertising -- almost everywhere a person turns someone is telling them *"How to..."* "How To" books are the easiest to sell nowadays and you're right, that's exactly what this book purports to be; a *"How to Think for Yourself"* book because there is no other way to succeed. I have heard, along with you, all the gurus contradicting one another in a constant stream; "Buy gold/Sell gold," "Get out of the stock market/Hang in there," "Buy term insurance/Buy whole life," "Probate is bad/Probate is good." Who can you believe; who should you follow?

The important thing to remember is that no one knows everything; even in his own field. Among doctors an eye, nose and throat man might not be up on the latest treatment for high blood pressure. A criminal lawyer may have little knowledge of the latest change in tax law. Even narrowed down, if you consult an ophthalmologist with your eye problem he certainly will not know everything there is to know about eyes. He will have a knowledgeable opinion; a judgment.

Do you then have to become an expert to recognize one? Remember that old kid's saying, "It takes one to know one!"? Well, that is the ideal and as impractical, impossible and ridiculous as it sounds, I am nevertheless advocating an approximation of it. You must be willing to research a subject enough to know the question to ask, the suggestions to make and have enough confidence in your own intelligence to evaluate arguments set forth on both sides. I defy you to think of an issue about which no one holds an opposing opinion! Do not be led blindly by last week's

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magazine article or this week's talk show guest. Check it out! In my experience the more dogmatic the individual the less intelligent and probably less informed.

If you want to take charge of your own life then you have some work ahead of you. You may even have to replace some television time with reading for nine months or so, but you'll become a more confident and self assured human being.

O.K. then -- let's get on with it!

Chapter Two
Goals

I find people don't think as *big* as they used to; they no longer try for the brass rings. Perhaps they're more realistic. But how do they know what is real till they give it a try? Each generation attempts to Americanize the English language. One of my favorite resulting phrases is "*Go for it*!" It's puzzling to me that the generation that coined that phrase seems less able to follow its dictates than earlier generations. It's hard to ask yourself what you want out of life when you start with unnecessary restrictions. What kind of twenty-three-year old would answer the question, "How much money would you like to me making at age thirty-five? with "$25,000.00"? Why not a million? Wouldn't he rather? Yes but-- but a lot of things. They know no one-- no family members or friends who are making a million dollars at age thirty-five. They hear of unemployment. They hear complaints all around them about the state of the economy. They end up doubting themselves and their abilities without giving themselves a chance.

Do we still want our kinds to have more than we did, or are we content-- resigned to the idea that they should and will have the same or maybe less than we who grew up in the 40s, 50s and 60s? Many of our parents were victims of the depression years so naturally they pushed for us to have more and do better.

I don't want to direct this book to any particular age group. The ideas here will work for you whatever your age and circumstances. The earlier in life you learn how to form and implement goals the easier it will be for you. Also I'm certainly not saying all twenty-three-year olds should have making a million dollars by age thirty-five as their goal! I am expressing amazement that they should restrict themselves to answering, "$25,000.00" on the basis of what they see and hear around them. "$25,000.00" may well be the answer I would encourage a certain young person to come to, but only after taking into consideration data such as in the following hypothetical:

Jon, age twenty-three does not want to marry until past age thirty, if ever. He is a teacher. He likes backpacking and things to do with nature.

"Hypothetical Jon" has no need for a lot of money. He anticipates no dependents, enjoys a profession which does not pay well and a non-working environment which is comparatively inexpensive. Jon, at this stage of his life, has determined that he values non-material things more than material. It just so happens that teaching and nature-loving complement one another; the profession providing both enough time and money to enhance the avocation. But even Jon has

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need of further planning and should read this book for information on insurance, passive investments, retirement planning, etc.

Those of us beyond age twenty-three may have seen ourselves when reading about Jon-- ourselves before we met our spouse and had several children! Planning can not be done once in a lifetime. That's it-- once and for all! The priorities in our lives change constantly. Our plans should be reviewed whenever an event such as a marriage, birth, death or career change takes place, and at any rate no less than once a year.

In forming goals of course, there are constraints. "*Go for it!*" means that more is possible than you may let yourself dream. That is the lack the majority of us have to overcome-- daring to dream! And even then most of us dare not soar, even in our imaginations. There is however, the other side which one encounters occasionally. The five foot six inch guy who wants to a basketball star; the 150 pound awkward large boned girl who dreams of becoming a prima donna on the ballet circuit; the person with 20/100 vision who always wanted to be a jet pilot, or even more tragic, the pianist who loses a hand; the painter who goes blind! One must learn to be realistic in forming goals and may on occasion need some objective feedback. I really believe nothing is impossible if one wants it badly enough, but an adjustment in planning may be in order. Vision can be corrected so one could fly even though the policies of the air force and commercial airlines prevent pursuing those two particular avenues as a career. Music can still be pursued with one hand; perhaps in composing, teaching or conducting. Dreams need not be scrapped when the unexpected intervenes; only a slight shift might be called for.

You should make friends with yourself. Get to know yourself. Your likes and dislikes; strengths and weaknesses. The questions at the end of this chapter are geared to help you do just that.

I have on occasion addressed the graduating classes at the Defense Language Institute in Monterey, California. I usually begin with a short story I heard some time ago. My version follows:

> In Berlin one day, a man, a detective, follows another man. He loses him; wonders if he has stopped at a particular hotel. To find out without causing suspicion, he decides that the best way is to go into the hotel, up to the desk clerk in the lobby and inquire if he himself (giving his own name of course) is registered there. While the clerk looks for his name on the register he plans quickly to scan the list to determine whether the other man he is pursuing is actually registered at the hotel.
>
> Everything works out according to plan-- at first. He enters the hotel, crosses the lobby, walks up to the desk and asks the clerk if he himself is registered there. Then he gets the shock of his life! Quickly, almost without looking at the register, the clerk says, "Yes, he is registered here and he is waiting for you in Room 1233." Stunned, the man backs away in a daze. Victim of his own scheming, he takes an elevator to the twelfth floor, and knocks on the door of Room 1233. Slowly the door opens. There, standing before him, is a man looking amazingly like himself-- a little grayer; a little heavier with a few more lines in his face-- the

> man he will be in about twenty-five years' time. I will leave their conversation to your imagination.
>
> The point being that for each of you there is a person- a YOU five, ten, twenty, twenty-five years in the future. When it is your turn to open that future door twenty-five years form now and look squarely in his eves, how will you like what you see?

I was going to start this chapter with the following words written almost 2,000 years ago by the Roman philosopher, Seneca: "Our plans miscarry because we have no aim. When a man does not know what harbor he is making for, no wind is the right winds." However, the more I thought about it the more I realized Seneca is generally but only partially right. He substantiates the importance of goals but Shakespeare realized life in the real world does not always work by cause and effect. Often the bad guys win-- unfortunate things happen to good people-- "Fortune brings in some boats that are not steered." (Shakespeare)

Sometimes one event leads to another, to another, in an almost gentle sequence.

As if one must get from step #1 to step #7 without seeming to do so. Somehow, psychologically or physically or because of lack of education or experience, if step #7 were presented directly to the person at step #1 it would be turned down flatly as a preposterous, unacceptable idea.

No matter how well you plan you cannot foresee all your future needs and wants. That's why the yearly review is so important. Some people will inevitably experience more changes than others. You do the best you can at the stage in which you find yourself. Use honest and thorough evaluations, and then prepare for the unexpected-- the unforeseen events which strike from time to time in all our lives.

Speaking of preparing for the unexpected bring us to the next chapter on risk management and the first mnemonic (pronounced with the first letter silent, "-nemonic" and meaning any memory aid). You will find mnemonics throughout the book. For those of you who don't find such devices useful the context of the book will not suffer if you simply choose to skip the pages which refer to mnemonics. I constantly use devices like the ones illustrated and have even written a separate book detailing their usefulness. If you are like me, a study of the mnemonics, usually presented here in the form of acronyms and visual aids, should help you retain and recall the information presented.

Keep a separate notebook for the information required by the worksheets found at the end of every chapter. That way you will have plenty of room for your answers and can keep in one place all the information you have gathered while reading this book.

Worksheet - Chapter Two

Self Test

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DO YOU KNOW WHO YOU ARE AND WHERE YOU ARE GOING?

This test is designed to help you know yourself a little better and define your goals.

DO NOT GENERALIZE -- BE SPECIFIC

1. My three best character strengths are_____.

2. My three worst character traits are _____.

3. My three best physical features are _____.

4. My three worst physical features are _____.

5. I used to be _____ but now _____.

6. I am satisfied with my educational achievements _____ or would like to pursue _____ and it will take _____ years.

7. If I could make three changes about my present job, _____, _____ and _____.

8. Most people see me as _____.

9. I see myself as _____.

10. I would be willing to work longer hours if _____ .

11. I would like to work less because _____ _____.

12. I don't mind taking direction as evidenced by _____.

13. I enjoy taking responsibility as evidenced by _____.

14. I prefer city to country living or vice versa _____

15. I prefer office work to physical activity or _____

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_____.

16. I would like to make _____ dollars next year, $ _____ in five years, $ _____ in 10 years, $_____ in 20 years.

17. My greatest achievement to date has been _____.

18. Taking risks is _____.

19. My feelings about SECURITY in home, marriage, job and money are _____.

20. If I could have 3 wishes which must be spent selfishly they would be _____, _____ and _____.

21. Name the ten public figures (sports, religious, political or from the entertainment field) you most admire and would like spend some time with.

_____ _____

_____ _____

_____ _____

_____ _____

_____ _____

Recommended Reading
Chapter Two

Make it a habit to read 1/2 hour of motivational material each day. I recommend anything written by :

Napoleon Hill	Erich Fromm
Norman Vincent Peale	Leo Buscaglia
Dale Carnegie	Og Mandino
J. Paul Getty	*Success*Magazine

The Magic of Thinking Big, by David Schwartz
How to Attract Good Luck, by A.H.Z. Carr
How to Give and Receive Advice, by Gerard Nierenberg

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Be the Person You Were Meant to Be, by Jerry Greenwald
Self-Renewal, by John Gardner
Advice form a Failure, by Jo Coudert
Shifting Gears, by Nena & George O'Neill
How to Live 365 Days a Year, by J.A. Schindler
The Art of Thinking, by Ernest Dimnet
A Guide to Rational Living, by Albert Ellis & Robert Powers
Only the Best, by Wallace Hildick
Success Forces, by Joseph Sugarman
The Psychology of Self-Esteem, by Nathaniel Branden
Psychomatics/The Power of Super-Persuasion, by Norvell
The Magic of Thinking Rich, by Ralph Charell
How to Get Rich Slowly but Almost Surely, by William T. Morris

Section Two
Risk Management

Chapter 3
Choosing Insurance

Believing in "Murphy's Law": "Whatever can possibly go wrong will," is the first step in determining risk.

A person has four choices when dealing with risk:

1. Accept the risk.
2. Avoid the risk.
3. Reduce the risk.
4. Transfer the risk.

ACCEPTING THE RISK

Accepting the risk is of course the most economical course as it involves doing nothing. That is the way you usually accept risks with very long odds and against which you feel powerless at any rate, such as nuclear war or chances of a meteor striking you or your property.

AVOIDING THE RISK

You choose to avoid the risk when you sell a property at a discount with no guarantees ("AS IS"), or a broker decides to have no salesmen because he does not want to be responsible for their actions, or a family decides against keeping a dog because of the possible harm it may cause to other people or their property, or one decides to take public transportation rather than drive to work to avoid freeway accidents.

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TRANSFERRING RISK

Transferring risk is the topic of our discussion. Transferring risk to a third party who agrees to take the risk form your shoulders in return for the payment of a certain sum of money, is what insurance is all about.

YOU AND YOUR POLICIES

Who reads an insurance policy? If I asked you what your limits of coverage are on your medical, health, homeowners or auto insurance could you tell me? Most of you are familiar with your deductibles. (The amount you yourself must pay before the insurance company pitches in.) Do you know what your health insurance elimination period is? (The time between the actual occurrence of the injury and the insurer's coverage actually takes effect.) Do you know you are covered by your own uninsured motorists provision of your automobile policy if you are a victim of a hit and run accident?

If your attitude is, "I leave that all to my insurance agent- we're friends, he's a good guy and I trust him," you are not alone and pardon me for saying so but you are a fool!

INSURANCE IS YOUR RESPONSIBILITY

It is not my intent to cast dispersion on insurance salesmen. The great majority of them are conscientious, do a good job and are indeed your "friend," a "good guy" and "honest"; that is not the point. You are a fool if you do not thoroughly investigate something which can play such a major role in your life plans. As well meaning as your professional may be, he is being pressured from several sides by his need to rise within his company, the economic needs of his family, the needs of many other clients to keep track of as well as his desire to give you quality service. As good as he may be no one knows your particular situation like you do.

HOW DO YOU CHOOSE YOUR AGENT

Choosing an insurance agent is much like choosing your other professionals, such as accountants, doctors, and lawyers. Initial contacts usually come about through referrals from friends or business associates. Service, conscientiousness and promptness are what you are looking for in an agent. You will also want a person you can feel comfortable with and whose personality is compatible with yours. Since you will be turning to him in times of trouble and emergency, you want a reassuring person who you can trust and confide in. In your agent has a designation such as a CLU (Chartered Life Underwriter), CPCU (Chartered Property Causal Underwriter), or CFP (Certified Financial Planner) it shows a commitment to his profession and a better than average degree of knowledge in his field. Although there are of course many competent and knowledgeable agents without any of these designations it should be noted that these titles are not given lightly and may take years to achieve by passing examinations on insurance, taxes and other related fields.

WHAT RISKS TO INSURE AGAINST AND FOR HOW MUCH

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All risks should not be insured against; it would be too costly. The risks that could potentially destroy your net worth are the ones to consider first.* It's not how often something occurs that one needs to be concerned about (for instance fender-benders to the automobile) but how large the damage could conceivably be (million dollar suit for personal injury payable to the other driver involved in the fender-bender).

A rule of thumb in determining whether to insure or retain the responsibility for paying potential losses in a given area, is to check out the relationship the potential claim bears to your family's current net worth. This would of course change over time. The larger your estate becomes the more important it is to have adequate liability coverage. Courts frequently award million dollar damages to plaintiffs nowadays.

People with limited incomes must choose their insurance wisely in order to cover the premiums (cost of coverage). For example, they may not be able to afford insurance on their house, the other fellow's automobile as well as their own and have complete health care coverage also. Since very often such a family's net worth is attributable mainly to their home, they dare not skimp on fire coverage so they may choose to absorb some medical expenses or damages to their own automobile. However, they should always make sure damage to the other fellow's car will be adequately covered so his attorney will not come against their home and other assets.

SUMMARY

Risk can be handled by acceptance (use when either threatened damages or likelihood of occurrence is slight), avoidance (refrain form certain actions or control over certain things), reduction (cultivate careful habits), or transference (the insurance company assumes your liability for a price). It's your responsibility to analyze your priorities and determine the coverage you need and can afford. It is foolish to leave these decisions entirely to your agent's discretion. Insure against losses that could wipe out your net worth rather than against those events that occur frequently but whose cost you can absorb without risking everything.

Fill out the form following this chapter to determine your net worth. Use a separate notebook so you will have everything in one place as suggested in Section One. The recommended reading list follows the worksheet.

* Your net worth consists of your assets, everything you own-- minus your liabilities which is all your debt.

Worksheet - Chapter Three

FORM TO DETERMINE NET WORTH
AS OF (DATE)_____

ASSETS

Liquid Assets

Cash and Checking _____

Savings accounts _____

Money markets _____

Life insurance-cash value _____

U.S. savings bonds _____

Brokerage accounts _____

Other _____

Total Liquid Assets _____

Marketable Invested Assets

Common stocks _____

Mutual Funds _____

Corporate bonds _____

Municipal bonds _____

Certificates of deposit _____

Other _____

Total Marketable Invested Assets _____

Nonmarketable Invested Assets

Business interests _____

Investment real estate _____

Pension accounts _____

Thrift plan accounts _____

Preferred stocks _____

Other _____

Total Nonmarketable Invested Assets _____

Use Assets (use fair market value)

Residence _____

Vacation home _____

Automobile _____

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Boat _____

Furs, jewelry _____

Furniture _____

Other personal property _____

Total Use Assets _____

LIABILITIES

Current Liabilities

Charge accounts/credit cards _____

Other outstanding bills _____

Short term loans _____

Outstanding taxes _____

Total Current Liabilities _____

Long Term Liabilities

Mortgage on residence _____

Mortgage on investment real estate _____

Auto loans _____

Other bank loans _____

Margin loans _____

Life insurance policy loans _____

Other _____

Total Long Term Liabilities _____

Family Net Worth
(subtract liabilities from assets)_____

Recommended Reading
Chapter Three

"Risk & Its Treatment: Changing Spocail Consequences, from *The Annals*, edited by George Rejda

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The Shoppers Guide Book, by Herbert Denenberg
The Great American Insurance Hoax, by Guarino & Trubo
The Invisible Bankers, by Andrew Tobias
Fundamentals of Insurance, by Robert Mehr
Principles of Insurance, by Geroge Rejda
Fundamentals of Risk and Insurance, by Emmett Vaughan
General Insurance, by David Bickelhaupt
Your Insurance Adviser, by Saul Sokol
Risk Management and Insurance, by Williams, Arthur & Heins
The Insurance Forum, by Joseph Belth
Best's Insurance Ratings, by A.M. Best Co.

Chapter 4
Health Insurance

The subject of health care costs is one of the most controversial topics in the country today. The Reagan administration, concerned by the sky-rocketing cost of health care, has proposed a combination of tax increases and limits on payments for services. All sorts of recommendations have been advocated by a host of conscientious citizens and politicians.

The medical surcharge is just one such proposal. Under this plan, a recipient of medical benefits from the government would be expected to reimburse the government according to his ability as determined by the amount of income tax he paid in a given year. The obligation to repay medical benefits would carry over from one year to another. If you received help when "down on your luck" when things got better (as evidenced by your income tax returns) your would be expected to pay off what would be considered to be a debt to the government. If you remain poor enough to pay no income tax you would never be expected to reimburse the government.

A Presidential Commission on the Study of Ethical Problems in Medicine and Biomedical and Behavioral Research, issued a report in the spring of 1983 entitled, "Securing Access to Health Care." They found 22 million to 25 million Americans had no health insurance coverage and that because of job changes or other reasons, approximately 34 million were without coverage at some point during a one year period. In this chapter we intend to analyze your individual coverage and see where you stand in this area.

BASIC MEDICAL COVERAGE

Basic coverage provides for hospital expenses, surgical proceedings and may be written to cover some health services outside the confines of the hospital. It was your common, and as the name implies, "basic coverage" for medical expenses until costs in the health field began to soar dramatically after the second world war. Because the maximum benefits are low and many expenses may not be covered, the consumer usually finds himself involved in patching several policies together in order to obtain anywhere near adequate coverage for his family. Because of these limitations major medical type policies are more popular today.

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MAJOR MEDICAL COVERAGE

Major medical policies have high or even unlimited maximum benefits which can be applied on a various time oriented base. Most types of medical care expenses are covered up to the policy's limits. However, major medical policies have what are called "inside limits' restricting coverage for certain items such as room and board, surgery and private nursing, to a specific pre-determined amount and no more. That amount is the "inside limit" for that particular policy. Because of the high maximum coverage these policies provide, the premiums would be out of reach for most people if deductibles and coinsurance provisions were not used. policies vary but the consumer is usually required to pay the first $100 or $200 of medical expenses (deductible) on either a calendar or benefit-year basis (the name is self-explanatory) or a per cause basis. Per cause means incident by incident. After the deductible is paid, the coinsurance provision normally provides for the insured to pay a specified portion of the covered expenses. An 80/20 coinsurance provision would require the insurance company to pay 80% of those items covered under a particular policy (N.B. not 80% of the entire bill) and the insured to be responsible for the remaining 20%.

The following illustration may be helpful:

MR. PAINE

Mr. Paine has a major medical coverage with a $100,000 policy limit (on a calendar-year basis) with a $100 deductible (on a per cause basis), an 80/20 coinsurance provision and an "inside limit" of $100 on a daily room and board and $35,000 "inside limit" surgical. Mr. Paine is hospitalized and his expenses are as follows:

Surgery	$40,000
Rm & Brd 100 days @ $125/day	$12,500
Other covered charges	$10,000
Total bill (within the $100,000 policy limit)	**$62,500**

The insurance company would pay:

Surgery (inside limit)	$35,000
Rm & Brd (inside limit)	$10,000
Fully covered charges	$10,000
Subtotal	$55,000
Coinsurance 80/20 (Sub x .80)	
Ins. Co. pays	$44,000
	$62,500
	- 44,000
Not reimbursed	**$18,500**

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"STOP-LOSS" PROVISION

The non-reimbursed portion of the bill ($18,500) in the previous example, would be tax deductible so the blow would be somewhat lessened depending on Mr. Paine's tax bracket. Better still would be a stop-loss provision that limits the insured's liability to a certain maximum amount each year. for instance, if Mr. Paine had a stop-loss of $10,000 per year per person in his policy, the insurance company would pick up an additional $8,500 of expenses. Mr. Paine would have his losses stopped at the $10,000 figure and would not be liable for more than that figure in any one year as far as his own medical expenses are concerned. This would be true even if his expenses reached the $100,000 limit-- the insurance company would have to pay $90,000 in such a case. It is evident that a stop-loss provision negates the coinsurance provision where catastrophic illness is concerned.

COMPREHENSIVE COVERAGE

Comprehensive coverage is really a combination of basic and major medical insurance. It usually requires smaller deductibles than major medical and deletes the coinsurance provision for certain basic policies.

EXCESS MAJOR MEDICAL

Excess major medical applies only after other medical coverage has been exhausted and when there is no stop-loss provision. In Mr. Paine's case, if complications arose it is conceivable his $100,000 limit could have been reached during a calendar year. Excess major medical is intended to cover catastrophic situations and should be considered when deciding on a total insurance package.

MEDICARE AND WORKERS COMPENSATION

Persons over age 65 are eligible for hospital insurance which includes up to 100 days of home nursing or nursing home care beyond the hospital stay. The supplementary medical insurance (SMI) will generally pay 80% of such persons' medical services after a $75/ year deductible. If you, or a family member, is 65 or over, be sure to read a more detailed account of the coverage provided under these programs. See the suggested reading list at the end of this chapter.

Workers compensation provides unlimited benefits to employees who are injured or contract an illness as a result of and while on the job.

GROUP INSURANCE

Group insurance is the most common type of coverage in the United States today. One can usually obtain broader benefits at a lower cost if one is covered as a member of a professional group, a service club or as an employee of a covered company. However, for a slightly higher premium one may join associations such as Blue-Cross Blue-Shield or Kaiser as a non-group subscriber and receive similar benefits.

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With both spouses frequently working nowadays, it is not uncommon to find oneself covered under more than one group policy; once as a subscriber and again perhaps as a dependent of a spouse. Group policies have provisions, however, limiting benefits to 100% of expenses covered so there can be no duplication or windfall for the insured covered under more than one group policy.

Normally children as well as spouses are covered under group plans and sometimes dependent parents are also included. Policies vary as to when benefits cease but the decisions are generally based on age and whether the child is handicapped or is still a full-time student.

RENEWAL PROVISIONS

Because one's health is likely to change over a period of time, a consumer should take a good look at renewal provisions when purchasing health insurance. There are three classifications to consider.

Renewal at the option of the insurer is the least desirable alternative from the insureds' point of view. The insurance company reserves the right to periodically reevaluate the insured in terms of possible deteriorating health and economic conditions in general. The insurer can cancel the policy, raise premiums and insert restrictions as to the future coverage offered.

The second category is the *guaranteed renewable policy* which prohibits the insurance company from canceling or changing coverage or raising premiums unless the entire class of policy holders is affected.

The most lenient renewal provision is the *non-cancelable ("non-can") policy* which gives the insurance company no right to make any changes in the consumers' coverage or premiums as long as the policy is kept in effect by the offer of timely payments.

Of course the trick when evaluating insurance is to weigh the cost against the privilege. In this case the more lenient the renewal provisions in a particular policy, the higher the premiums will be. However, the higher cost may well be worth it to a consumer who anticipates failing health because of family history or some other reason and therefore does not want to risk being turned down for coverage in future years or having to pay prohibitive premiums for inadequate coverage.

SUMMARY

Basic medical coverage is limited as to the benefits provided and has relatively low policy limits in this age of soaring health care costs. Most people find major medical coverage preferable and almost necessary. High limits on benefits are possible by using deductibles, coinsurance provisions and inside limits to bring the premiums within the range of most consumers. Coupled with stop-loss provisions, the risk of catastrophic illness is adequately eliminated. There are many providers of health insurance but group plans are the most popular. The majority of workers receive some such coverage for their families through their employment. Often premiums are paid by their employer as a fringe benefit of the workplace. You should familiarize

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yourself with the provisions of government policies such as workman's compensation and Medicare. Make sure you check to see exactly what the renewal provisions are before you buy a particular policy and weigh the benefits to your specific situation against the cost.

Fill out the following worksheet (in your special notebook) and check out the reading list at the end of this chapter.

Recommended Reading
Chapter 4

The Consumer's Book of Health, by Jordan Braverman
Life and Health Insurance Handbook, by Gregg & Lucas
The Medicare Answer Book, by Geri Harrington
The Corner Drugstore, by Max Leber
"Health Policy: The Legislative Agenda" and "National Health Issues." both by *Congressional Quarterly, Inc.*

For information you might write to:

Public Citizen Health Research Group
2000 P Street N.W.
Washington, D.C. 20036

Consumer Coalition for Health 930 F Street N.W.
Washington, D.C. 20004

Medicine in the Public Interest
65 Franklin Street
Boston, Massachusetts 02110

Chapter 5
Unemployment Insurance

Government Controlled Unemployment Insurance

The Act

The Federal Unemployment Insurance Act, like Social Security and other social programs, was a product of the depression ridden 30s. Originally benefits were extended only to certain groups of workers and those persons Congress felt had been "unjustly" laid off work through no fault of their own.

During the fairly recent economic recession of 1975 the "safety-net" was extended to provide benefits to farm workers, domestics and others who had been left out when the original Act was implemented.

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CALIFORNIA AS AN EXAMPLE

You can pick up a booklet, and should do so, at your local unemployment office, which will explain the benefits you are entitled to if you should lose your job. The states, while conforming to federal guide lines, have varying rules for eligibility and benefits. There are more than two hundred offices to help you in California.

To find the one nearest you look in the telephone book under California State of Employment Development Department.

You should file for benefits immediately upon losing your job even though there is a one week elimination period (waiting period before you become eligible to receive benefits).

In California you may normally receive benefits up to 26 weeks in a 52-week period and for an amount equal to roughly one-half your former weekly pay. A table in which you can find your specific benefits (as well as more detailed information) is found in the booklet provided by the State.

TRULY AN INSURANCE POLICY

Like any insurance policy, money (premium) is paid to the insurer (government) periodically, so that it is available to an employee should he find himself without a job. Like some group health insurance policies, the premium is paid by the employer not the

employee (beneficiary) who receives the benefits. The one big difference is that whereas health insurance is an optional fringe benefit provided as a supplement to wages, unemployment insurance is a mandatory payroll tax in order to fund the program. There are exceptions and modifications to this broad statement. If you consult the recommended reading list at the end of this chapter you will find suggestions on where to get more details. If you live in Alaska, Alabama or New Jersey there are unique rules in your state so be sure to check with your appropriate state agency.

THE BEST INSURANCE AGAINST UNEMPLOYMENT

The best insurance against unemployment is to have several skills and alternate sources of making an income.

CHOOSE YOUR EMPLOYER WITH CARE

It is foolish to be totally at the whim of an employer. Even a healthy business in a stable economic environment can go bankrupt. It is not uncommon to hear of a situation where a son or other family member takes over the business after the founders' death and through lack of care, skill or perhaps with a subconscious revenge, runs the enterprise right into the ground! That is the type of situation an employee cannot guard against just by making an initially wise choice of employers. Even the right industry, at the right time with the right employer can end up wrong with the passage of time. Ask the aerospace engineers in Seattle in the 70s.

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WE CAN'T FORESEE THE FUTURE

The whole science (art) of risk management is premised on the unforeseeability of the future. Precisely because we don't know that tomorrow will bring we must be prepared for the worst. If we could fast forward our lives and see that our house would not be broken in to or suffer a fire or that the entire family would escape ever being involved in an automobile accident, we could immediately cancel our auto and fire insurance coverage and pocket the savings in premiums.

OFTEN OVERLOOKED RESOURCES

It is amazing how many resources the average American has to fall back on if he should lose his job, and he may not even know it!!

IF YOU WERE TAUGHT YOU CAN TEACH

Did you ever take lessons when you were a kid? Lessons in what, you might ask. Anything you can imagine! Musical instruments, voice dance, exercise classes, gymnastics, sailing, flying, swimming, high diving, scuba diving, wind surfing, drama, ceramics, art, leather work, woodcarving, ice or roller skating, skiing, archery, sharp shooting, cooking, sewing, writing, martial arts, boxing, etc., etc.

Chances are, if your were taught you can teach. Try and remember how it was done. If you're not sure how to start someone out, take a few lessons now, or sit in on the lessons of your own child, friend or neighbor. Make sure you get permission from the pupil and teacher first.

PUT YOUR SKILLS AND TALENTS TO WORK FOR $$

Of course not all people make good teachers but talent and skills can be used to bring you income in other ways. Perhaps your music lessons "took" and you have kept your proficiency high enough to get a job as a musician in your area. Try "moonlighting" at first on certain nights or on weekends. Maybe you can organize your own group. If you tend toward the more classical approach you might get a job playing the organ at a local church or giving recitals several times a year.

If you have a boat or plane you might take tourists out on weekends for a pleasure excursion. (Make certain you charge enough to at least cover the insurance which may well be too high for a part time business to handle.)

Of course the products of many of the skills you have acquired could be retailed. We all know about the successful pottery or woodcarving business that started as a basement hobby.

I haven't even mentioned the sills that are not formally taught but that you may have picked up over the years in an attempt to save yourself money and because you found you were good at it and loved doing it. I'm referring to plumbing, carpentry, painting, auto mechanics, gardening, etc.; the skills the rest of us depend on and for which we are willing to pay "big bucks"

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YOUR FAMILY AS AN EMERGENCY ASSET

By now you should be looking at yourself and your family in a different light. You might be seeing dollar signs on Judy's cinnamon rolls that have won first prize at the fair the last seven years. Molly has been taking piano lessons since she was five. She could probably teach the neighborhood children she now baby-sits for and for a lot more money. Son Jeff can fix anything; toasters, TVs, vacuums. He could advertise his skills and get paid.

You may understandably not want to exploit (what a "loaded" word) any

of these talents. I hope you are comfortable at the moment and enjoy being the guy whose son can fix anything for your " all thumbs" associates at the office. I understand that it gives you a feeling of pride when everyone asks for Judy's baked goods when a party is being planned and would just love it if you could only coax Molly to play a few pieces.

Fine! That's the way I hope your life will remain. But remember these skills are also insurance.

NO AFTER-SKILLS OR HOBBIES?

Is it possible you've read this far and don't see yourself or family in any of the illustrations? Highly unlikely but possible. It could be you, the reader, are unattached with no present family and have buried yourself in your one and only job. Even if you've never had a lesson in your life, have had no time for hobbies, know nothing about cars and live in an apartment where all the maintenance is taken care of by picking up the phone, you can still acquire "unemployment insurance" in a myriad of ways.

WAYS TO ACQUIRE THE SKILLS NECESSARY TO INSURE AGAINST UNEMPLOYMENT

THE INSURANCE THAT PAYS YOU TO GET IT

The government, through the National and Coast Guard and other branches of the military, have Reservist programs. As a reservist, you can learn, at the government's expense, just about any skill imaginable by applying for the desired training. Once more, you do not pay to get this sometimes highly technical and potentially lucrative knowledge, rather you are paid to learn! This training need not interfere with your present employment. The time required as a Reservist is usually a weekend per month and a few weeks at a time for the extensive training sessions which can be arranged with your employer. Chances are your employer will be proud to have a Reservist in his employ. Such as an affiliation is more likely to help rather than hinder you in your present career. At any rate, by law your employer must give you the needed time off and cannot discriminate against you because of your Reserve status.

COMMUNITY COURSES

Be on the lookout for free courses offered in your community by the YMCA, Red Cross, City or State College and other public oriented and sponsored organizations.

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KNOWLEDGE FOR A FEE

Many trade schools offer night classes. You can earn credentials which qualify you to work in any filed. You could qualify as an assistant in the medical or legal field or learn to program and work with computers. It never hurt to have a real estate or bartender's license in your back pocket. It's possible to qualify as a contractor or accountant by hitting the books hard. If you're willing to put in even more study after your regular work day, there are night law schools and university extension courses in most communities which allow one to obtain academic degrees. A fee is usually charged as tuition. A license or other evidence of your competency is only presented after the successful passage of one or more, sometimes rigorous examinations.

This type of insurance is not for everyone. However, you should know it is available to you.

It's crazy to cry about lack of opportunity or equality in this country when it is all around you. There is nobody who could not give up their regular TV time for study and could not raise tuition and book money by working at one of the fast-food restaurants in town that are always sporting a *Help Wanted* sign. Minimum wage jobs could be temporary if you use them to advance your position.

CORRESPONDENCE - KNOWLEDGE BY MAIL

I was approached by a member of the audience once after a speech in which I had alluded to correspondence courses. "I have seen advertisements in magazines for years," he said, "but until today I thought those mail order degrees were a hoax." Perhaps some are; but what amazed me is the apparent desire he suddenly had to pursue such a course since I had endorsed them and pointed out their merits. He had not written for any information from the advertisers in an attempt to prove they were charlatans he just thought they were! Likewise, he seemed content to accept my word that they were OK without doing any checking on his own. It is possible he might hit upon an unethical outfit and not get value for his time and money.

The point I am making and will make again and again throughout this book, is that you cannot go blindly through life with any degree of efficiency and success depending on your own vague unsupported feelings or the unverified word of others. Chart your own course; don't leave it to others!

SUMMARY

Obtain information form your State Unemployment Office *before* you need it. If you are familiar with the procedures for eligibility and amount of benefits available in your state you can plan your other insurance around these benefits.

The best unemployment insurance is self reliance. Don't let the security and happiness of yourself and family depend wholly on your present employer. Have alternate plans made for supporting your present life-style. Keep those skills and talents honed to a fine degree and acquire others if necessary.

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When Aristotle was asked the advantages of learning he replied, "It is an ornament to a man in prosperity, and a refuge to him in adversity." I rest my case!

Worksheet - Chapter 5

UNEMPLOYMENT INSURANCE
TO HELP YOU ANALYZE YOUR ASSETS

Make a separate list for each member of the family.

Have you had lessons in:

A musical instrument? (list them all)
Voice? Leather work?
Dance? Woodcarving?
Gymnastics? Ice skating?
Sailing? Roller Skating?
Flying? Skiing?
Swimming? Archery?
High diving? Marital arts?
Scuba diving? Boxing?
Wind surfing? Cooking?
Drama? Sewing?
Ceramics Writing?
Art? Other?

List any marketable sills or hobbies not mentioned above.

Such as:

Plumbing Auto mechanics Gardening
Carpentry Painting Typing -- Office skills

Make a list of all licenses, credentials and academic degrees.

List all the jobs you have ever held from age 14 on.

CONGRATULATIONS!

Recommended Reading
Chapter 5

The Unemployment Benefits Handbook, by Peter Jan Honigsberg
Your Legal Guide to Unemployment Insurance, by Peter Jan Honisberg

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America in Transition; Implications for Employee Benefits, by EBRI (Employment Benefit Research Institute)
Earning Money Without a Job, by J.C. Levinson
Earning Money at Home, by Peter Davidson
How to Make Money at Home, by Shebar & Schoder
100 Ways tp Make Money in Your Spare Time Starting with Less Than $100, by John Stockwell & Herber Holtje
184 Business Anyone Can Start & Make a Lot of Money, by Chase Revel
Sparetime Businesses You Can Run for Less than $1,500, by Scott Witt
How to Make Big Money in Your Spare Time, by Scott Witt
Sell Your Photographs, by Natalie Canavor
Career Opportunities in Crafts, by Elyse Sommer
How to Earn $15 to $50 an Hour with a Pickup Truck or Van, by Don Lilly
Entrepreneur Magazine
How to Publish Your Own Book, by L.W. Mueller
How to Start Your Own Small Business, published by Drake
The Crafstman's Survival Manual, by George & Nancy Wettlaufer
How to Start Your Own Craft Business, by Genfan & Taetzsch
Earn Money at Home, by Peter Davidson
Moonlighters Guide to a Sparetime Fortune, by Richard Michael
Turn Your Kitchen into a Gold Mine, by Alice & Alfred Howard
Working Free, by John Applegath

Chapter 6
Disability Insurance

Disability is something that always happens to the other guy. I have no trouble with that thought-- it shows a good healthy optimistic attitude. In fact, if one seriously believed he was fated to be one of the disabled it would be hard to function. Everything we do has some element of danger about it. If we thought we were the one destined for permanent injury it would be hard to force ourselves to fly in an airplane, go on a freeway, turn on our furnaces, use power tools, etc., etc. We would naturally want to *avoid the risk* of disability, but it cannot be done while we still live a normal productive 20th century life. We must be content to only *reduce the risk* of disability by prudent living. We can, however, transfer to insurance companies the monetary risk that may be connected with a disability. In this chapter we will explore the ways we can use insurance to minimize disability caused income losses.

WHAT IS A DISABILITY

There are three definitions of a disability commonly recognized by insurers.

The *"own occupation"* definition states that a person is considered for coverage purposes when he is no longer able to engage in the duties pertaining to the occupation for which he was trained and at which he was previously employed. This is the most lenient definition from the insured's viewpoint. Smile if your policy uses this definition!

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The *"any occupation*" definition is stricter and makes it harder to qualify for benefits. A person must be unable to engage in any gainful occupation whatsoever. This is the definition used to qualify persons for social security disability benefits as well as being found in some private policies.

The *"split definition"* is really a combination of the other two. Usually the "own occupation" definition is applied to the situation for a period of time and then the " any occupation" definition is used.

KINDS OF INSURERS

This government, through workman's compensation and social security, is the largest insurer of disabled workers. A few states, including California and New York, also have non-occupational disability benefits which provide benefits for relatively short periods of time.

Group insurance is another source of disability coverage often provided by employers for their employees.

Individual policies are available for those who are not members of a group or to supplement other coverage. Disability provisions are frequently found in pension and retirement plans and as part of other insurance policies as in auto, homeowners, hospital and life insurance. Read your policies carefully to determine the existence and extent of any disability coverage you may have missed. The worksheet at the end of this chapter will give you a clear picture of your coverage from combined sources.

WHEN DO BENEFITS BEGIN AND END

The time that occurs between the injury accident or onset of illness and the actual initiation of benefits is referred to as the elimination period. The *elimination period* for social security benefits is five months. For other coverage the time can carry from as little as seven days for illness and immediate benefit for accident, to a one-year elimination period for both accident and illness! The shorter the elimination period, of course, the higher the cost. Longer elimination periods result in savings on premiums.

Benefits can last anywhere from six moths to the insured's lifetime for accident-caused disabilities or to age sixty-five for disability due to illness. That's when pension and government benefits take up the slack.

COMMON PROVISIONS

Even though we think of disability occurring mainly as a result of accidents, coverage should definitely include disability due to illness as well. A policy covering accidents only is too restrictive and even though it costs less it does not provide adequate coverage.

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Some policies have provisions requiring that the disabled person be confined to the indoors during the benefit period. These are often called "prison clauses" and should be avoided. It could be psychologically defeating to know your benefits would be in jeopardy if you left your house!

" Coordination-of-benefits provisions" are found in most group disability policies. Benefits are usually reduced by the amount of benefits payable under government disability policies and, but not because of, benefits payable under individual disability income insurance.

There is usually a minimum period of employment required before a person qualifies for coverage under an employer sponsored disability plan.

Most group plans cover non-job related injuries as well as disabilities contracted on the job. This is commonly referred to as "24 hour coverage".

Sometimes provision is made for payment of partial benefits for partial disability.

Provisions for guaranteed insurability, waiver of premium and double indemnity type clauses are found in many disability policies but since they are more commonly associated with life insurance they will be discussed in Chapter Seven.

WHO IS ELIGIBLE FOR COVERAGE

Obviously any consumer who purchases a policy or is insured by his employer or through membership in a group, can obtain coverage. Government insurance is almost automatic. If you are injured in the workplace you are covered by workman's compensation. Disabilities ("any occupation" type) are automatically covered by social security wherever they take place. A person may also be eligible for benefits because of his relationship to the disabled party; i.e. because he is a spouse or dependent.

BENEFITS (monthly)

Social security disability benefits are computed on a formula involving the disabled person's former salary and number of dependents he has and their ages. There is a maximum amount of coverage allowed per family. These benefits are tax-free from the federal government.

Group plans pay benefits determined by computing a percentage of the insured's base salary up to predetermined maximums. For example, 60% of salary up to $2,000/month.

Individual policies can be purchased in any amount the consumer can afford within certain limitations set by the particular company. Insurers have "issue limits" which determine the maximum amount of monthly coverage they are allowed to write on a person. "Participation limits" are restrictions on the amount of coverage on any one individual that a company, according to its rules, is allowed to participate in writing along with other insurers. Naturally the limits for participation with other companies is larger than the issue limit would be. For example, an insurer might have an issue limit of $2,000./month and a participation limit of $3,500/month.

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HYPOTHETICAL MR. PAINE

Another visit to Mr. Paine may prove useful at this point.

HYPOTHETICAL

Mr. Paine has been employed as a professional soccer player at a base salary of $48,000/year for the past two years. One night when coming home form a party, he was involved in an automobile accident which left him paralyzed for life from the waist down. He had dropped out of law school, not for academic deficiencies, but because his soccer skills were in great demand and he could not resist the temptation to cash in on his extraordinary talent. His disability coverage as a member of the soccer team was as follows: He was eligible to receive benefits under the plan after 18 months employment: the maximum benefit is life for accident-caused disabilities and to age 65 for illness; the elimination period is three months for accident and six months for illness; the coverage is "24 hour" (occupational as well as non-occupational); the definition of disability is "split," first five years "own occupation", remainder "any occupation; the benefits to be paid are to be based on 50% of covered employee's salary up to a maximum of $2,500/month.

An analysis of his benefits follows; Mr. Paine has met the 18-month eligibility provision because he has been with the team for two years. Since his injury was the result of accident, his benefits could conceivably continue for the rest of his life under this plan depending on the outcome of other determinations. He would have to wait three months until benefit payments would begin under this policy (elimination period and benefits would not be retroactive to the date of the accident. Since the coverage is "24 hour" it is irrelevant that the injury was not work-related but rather occurred coming home from a social engagement. Under the "split" definition used in this policy Mr. Paine would be eligible for benefits if he cannot engage in his "own occupation" for five years. He would therefore receive those benefits for that period of time. Under the "any occupation" definition to be applied after the five year period is terminated it is likely that Mr. Paine will be declared ineligible for benefits. There are many occupations which do not require the use of legs and for which Mr. Paine would probably find himself qualified. Among those is the practice of law for which Mr. Paine was partially trained. According to this policy, during his five years of apparent eligibility Mr. Paine should receive 50% of his base salary or $2,000/month. ($48,000/year 12 = $4,000/month, 50% of which is $2,000).

Because group plans coordinate benefits it is likely the insurance company would have those payments cut in half due to approximately a $1,000/month benefit Mr. Paine would be receiving from social security disability coverage.

SUMMARY

It is wise to look at disability coverage in the light of your insurance package. You may find you are covered under multiple sources such as workman's compensation, a group plan, individual supplemental and perhaps auto or liability policies your own or a third party's . You must check the coordination of benefit provisions along with the various elimination periods. Analyze your policies carefully to determine the definition of disability used in each case, the perils covered, the extent of the benefit period and the amount of benefit dollars available to you as compared

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with your normal and hoped for standard of living. If you find your present anticipated benefits would be inadequate but you don't want to add to your premium costs, consider setting dollars aside to invest in an emergency fund.

If you diligently fill out the worksheet at the end of this chapter you may be pleasantly surprised by unveiled coverage you didn't suspect you had.

Consult the recommended reading list if you have more questions and of course your own individual insurance agent, who, by the way, should find it a delight to discuss insurance with a client who knows the terminology, the questions that need asking and is able to understand a direct answer rather than depending on the old reassuring platitudes like: " Don't worry. I'll take care of everything." For some of you that was possibly the extent of your former communication with your insurance professional. How does it feel to be in control?

Recommended Reading
Chapter 6

How to Stay Ahead Financially., by Phillip Gordis
Jobs for the Disabled, by Sar Levitan & Robert Taggart
The Rights of Physically Handicapped People, by Kent Hull
The Source Book for the Disabled, by Gloria Hale

Chapter 7
Death Prematurely Life Insurance

LIFE INSURANCE AS AN ESTATE SUBSTITUTE

In your 20s and 30s when you are likely to have many dependents and few material assets, life insurance serves as an effective estate substitute. In the event of your premature death, your life insurance would provide economic support to those left behind.

LIFE INSURANCE AS AN ESTATE BUILDER

In your 40s and 50s you probably have already acquired a home and other substantial assets. Now life insurance should be viewed as a savings and investment tool that helps build your growing estate.

LIFE INSURANCE PROVIDES ESTATE LIQUIDITY

In your 60s and 70s you have few dependents and a well built up estate. At your death your spouse will be taken care of by social security, pensions or other retirement funds. Life insurance, a protection against premature death, should now provide liquidity for your estate during probate. (A more in-depth discussion of insurance for this period of life is covered in Section Six.)

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KINDS OF LIFE INSURANCE

There are many kinds of life insurance as the mind of man can conceive. For the sake of brevity we will discuss three arbitrary categories; individually purchased policies, group insurance and government sponsored coverage.

INDIVIDUALLY PURCHASED INSURANCE

Term. This kind of insurance affords the greatest projection for your dollar. Because it is the most inexpensive kind of coverage, young people with limited financial resources often find term insurance meets their short range needs. Term insurance is purchased for a specific period of time. There is no cash value build-up over time; the entire premium goes for protection. It is sometimes used to supplement other policies or when extra protection is desired temporarily. Since no portion of the premium is set aside as savings or investment, it is possible to purchase a high dollar amount of coverage for less than a lower dollar coverage would cost for other types of insurance. Premiums can be paid at a "level" amount over the term of the policy or in "decreasing" amounts if coverage needs decrease over the same period of time.

Whole Life. Whole life insurance, as its name implies, is coverage for the whole life of the insured as opposed to a specific period of time (term). Payments (premiums) do not necessarily have to continue over the life of the policy (which, by the way, corresponds to the life of the insured) but if they do, the policy is referred to as a "straight" or " ordinary life" policy. If premiums are to be paid only until the insured attains a specified age or for a certain number of years, the policy is called a "limited payement" policy. It differs from term insurance in another important way. A portion of the larger premiums is set aside with each payment as a savings account. The build-up of this "extra" premium keeps compounding interest over time and results in a cash value far beyond what is paid in. Of course the cash value of the policy varies at any given point in time.

Whole life insurance is probably the most popular form of life insurance for those who can afford the premiums because it combines savings with protection.

In the last several years all sorts of policies have arisen with ways of using the savings portion of the premium for investments (variable life policies) or tailoring the size of the premiums to the desires of the consumer; i.e. allowing smaller payments during anticipated leaner periods of the client's life, etc.

Premiums can be paid monthly, quarterly or any convenient way you and your agent agree upon. The most economical way, if you can do so without significant hardship, is to make annual payments. That way your premium will be compounding interest from the beginning of the year and there will be no "service charge." It may also be useful to note that it is less expensive to buy one large policy than several small policies.

Endowment. An endowment policy is another type of savings accounts. Although it insures against death for a specified period of time rather than for the whole life of the insured, the

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premiums are higher than term insurance premiums, the extra cost going into the build-up of a cash value. Endowment policies are actually a hybrid of term and whole life insurance.

GROUP POLICIES

Group policies have been mentioned earlier when discussing health and disability insurance. This kind of life insurance has the same characteristics earlier noted in group plans. Premiums are usually lower than individually purchased policies thanks to group

rates. When provided by an employer, group life insurance is considered a fringe benefit. Another feature which distinguishes group policies from individual life policies is the fact that evidence of insurability is not required; i.e. there is no necessity for a qualifying medical examination as there is when you apply for an individual life insurance policy.

GOVERNMENT SPONSORED LIFE INSURANCE

Social security, while not commonly thought of as life insurance, is really just that. It provides benefits to the family of a deceased worker through a formula determined by taking a percentage of what the insured would have received as retirement benefits had he reached age 65. You should familiarize yourself with eligibility requirements and benefits. For more detailed social security information consult the reading list at the end of this chapter.

Another government sponsored life insurance program is SGLI (Servicemen's Group Life Insurance) which in 1965 replaced older service related programs. It provides inexpensive coverage for persons on active duty in one of the services. I would advise anyone with an eligible family member to check with the respective service for more information.

A COMMON RIDER FOR PEOPLE WITH YOUNG FAMILIES

There are many variations of the "family income" life insurance policy or rider. People with young children should discuss with their agent, the desirability of obtaining this special coverage.

Basically a policy for a certain amount is purchased to cover the period when the children are dependent. The insurance company is obligated to make payments to the beneficiaries of $10, $15, or $20 for each $1,000 of face amount if the insured should die before the time period is up. For example; if the insured should die four years after purchasing a policy which was written for $70,000 over a 20 year period at $10 per $1,000 the surviving family would get $700 per month for 16 years (20 yr. term minus the four years the insured lived after purchasing the policy) and $70,000 face amount at the end of that time. The coverage combines a basic whole life insurance policy with a term coverage, either decreasing or level depending on the particular variation. It is a popular form of coverage and may provide just the projection you need if you are a young person starting to raise a family. Of course it costs more than term insurance. Your particular financial circumstances must be considered by you and your agent or other professional planner to determine if it should have a place in your financial plan.

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DIVIDENDS

Dividends are issued only by *participating* life insurance companies. These companies can be regular stock companies or mutual companies where every policy holder owns a piece of the company; a co-op system. In order to issue a dividend the company must charge premiums in excess of what is actually distributed to its holders as death benefits. The amount of dividend, if any, is determined on the mortality rate of its presently insured participants as well as on how efficiently the company is managed and how well its investments have done. All mutual life insurance companies are *participating*.

The stock companies that are *not participating* charge a fixed rate for their premiums. The premium is calculated to cover all expenses with no "extra" to be refunded in the form of dividends. It is not possible to determine in advance which type of policy will be cheapest in any given year. When the dividend of a participating company is small the fixed premium of the non-participating company would save you money. On the other hand, in a year with high dividends returned to policy holders, the participating company would be your best bet.

WHAT HAPPENS WHEN YOU STOP MAKING PREMIUMS?

Term life insurance coverage is similar to putting your dime in a dryer at the public laundromat; when the time paid for runs out, the dryer stops. If you want more drying time you pout more money in the dryer. Under the provisions of term life insurance contracts, when payment stops, the coverage simply terminates. After all, you were only paying for a certain period of coverage.

Whole life coverage with cash value poses a different problem. If for some reason you can no longer continue paying premiums do you lose everything that has been built up over time?

The answer is *no*. A choice that is always open to you is to cancel future protection and take the cash that has accumulated in the policy up to that point in time. A second alternative is to reduce your amount of coverage and replace your former policy with a newer smaller paid-up policy. However, if you sill need the full amount of coverage provided by the original insurance policy, you can buy a paid-up term policy instead. Just how long a term you can purchase will be determined by the cash value of the old policy and your age at the time of the conversion.

USING YOUR WHOLE LIFE POLICY AS A FINANCIAL TOOL

It is always possible to borrow against the cash value of your whole life insurance policy if you should need cash for any reason.

TO MAINTAIN PREMIUMS

It may be wise to include provision for an automatic premium loan in your policy. When a premium is not paid the premium amount is automatically deducted from the cash value. An agreed upon interest rate is charged, usually below market rates. The loan can be paid back at

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any time, and should be whenever possible, because if it is still outstanding at the insured's death the proceeds due the beneficiaries will be reduced accordingly.

GRACE AND REINSTATEMENT PERIODS

It should be noted that there is usually a thirty-one day grace period which keeps the policy in full force during this time even though the premium is overdue. This is useful to cover inadvertent lapses.

Even when the grace period has ended, the insured generally has three years to reinstate the policy without losing any benefits. The payment of all back premiums is required as well as the ability to show evidence of current insurability.

You might say, " Why not get a new policy and save all those back premiums?" If you had taken out the policy and had been making payments for twelve years before you found yourself unable to continue, you would be (counting the reinstatement period) at least fifteen years older and subject to higher premiums because of your age.

There are numerous other reasons that would make your older policy more desirable than starting again with a new policy. For instance, you don't have to start all over building a cash value from day one; your older policy may have better interest rates, as well as options and other liberal provisions no longer available in a new policy.

COLLATERAL

Beside taking loans against the cash value of the policy, the policy itself may be offered as collateral for a bank or other commercial loan. If the loan amount is not paid back according to the terms of the agreement, the lender becomes the owner of the policy. Of course any person or entity can become owner of a policy insuring the life of a third party as long as he can show an insurable interest. Indeed, this is often advisable, as we shall see when we discuss probate costs in Section Six a little later on.

HOW MUCH LIFE INSURANCE SHOULD YOU PURCHASE?

The worksheet at the end of this chapter will help you make this decision. After the insured's death there are special, continuing and future expenses which must be calculated in dollar terms. The object is to ensure the deceased's family can live in the manner they are used to or could have looked forward to had the deceased not died prematurely.

Because of the constant changes in laws and the uncertainty some people feel about social security, you may want to calculate needs without taking government insurance into consideration. Of course, if all goes well, you will be that much ahead. However, to plan without relying on governmental promises you must be willing to stretch, if need be, to afford the larger premiums necessary for higher coverage. Don't forget to take into consideration other

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investments and possible inheritances which may make extra dollars available when the kids are ready for college, for example.

Some planners suggest a rough calculation, you should have life insurance coverage equivalent to five years expenses; that being the time thought necessary for a family to "get back on its feet." Unfortunately the determination is not as simple as that. If you are not mathematically inclined, you may need help in figuring future values. Inflation, interest compounding and time must all be figured to determine the amount of insurance that will cover your future needs in terms of future dollars. your insurance agent or other professional can do the calculations for you once you have gathered the information. After all, that is the purpose of this book and especially the worksheets; to help you gather information for consultation with your professional at a reduced fee.

DESIGNATING BENEFICIARIES CAN BE TRICKY

In most cases the insured is the owner of the policy on his own life and as such reserves the right to appoint and change the beneficiary of the policy at any time up to his own death. We will see in our discussion in the Section dealing with Estate Planning, why this arrangement is not always desirable. For now, however, let us concentrate on who these beneficiaries might be.

Most often the spouse is designated as beneficiary with children as contingent (alternate) beneficiaries. It is always wise to appoint more than one beneficiary in case the first appointed fails to survive the insured. It is also a good idea to name the beneficiary as well as adding a descriptive phrase. For instance; Mary Smith, if she is my wife at the time of my death." If you simply say, "Mary Smith" or " to my wife", she may have divorced you and is now known as Mary Jones and the wife of another. To you, "my wife" means the person you are married to at the time of your death but legally this is not clear. The law cannot distinguish from those two words whether you refer to the woman you were married to when the policy was written or the woman you may have subsequently married.

Because of the technical difficulties so often encountered in this area, I would urge you to get an attorney to look over this important aspect of your policy. The small fee involved is nothing compared to the court costs which are a natural product of such ambiguities.

INSURANCE PROCEEDS

There are several alternatives to receiving life insurance proceeds all at once; i.e. in a "lump sum."

INCOME FOR LIFE

The income for life option is similar to a normally purchased annuity. Here, in exchange for letting the insurance company have the use of the proceeds due you as beneficiary (as a result of an insured's death) the company promises to provide you with an income for life. If you, as beneficiary, are in poor health this would, of course, be a foolish option. Even if you are relatively young and in excellent health you might be able to make better use of the insurance

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proceeds yourself. It may be possible to generate a better cash flow through sound investments than what the insurance company is offering. Before opting to receive proceeds under a "for life" plan, weigh the consequences carefully. Once proceeds begin to flow it is too late to make a change. The life income option may take many forms:

Pure life income. The pure life income option provides the highest monthly income. The company simply promises to pay a predetermined amount each month to the beneficiary until his death. Since there is no provision for "refunds" it is quite possible the insurance company can come out way ahead. If the proceeds are large the monthly income payments must be equally large in order to use up the proceeds during the beneficiary's lifetime. When the beneficiary dies before all the proceeds are paid the insurance company "pockets" the remainder. On the other hand, the beneficiary could come out ahead if he could mange to outlive the proceeds. In such an event the insurance company would have to dip into its own "pockets" to come up with the promised monthly payments. But don't bet on it; the payments are pre-determined to avoid just such a catastrophe for the insurer!

Refund Option. Under this option, if you choose to receive smaller monthly payments for life, any proceeds remaining at your death would be "refunded" to a predetermined third party; either in a "lump-sum" or in installments.

Minimum Time Period Option. Electing this option would guarantee the beneficiary monthly payments for life (again, smaller payments than under the "pure life income option") but in no case for less than a certain amount of time. If you, as beneficiary, didn't outlive the "certain time" agreed upon, monthly payments would be paid to a designated third party until the specified time period was met. The insurance company would still be ahead here, but not as much as in a pure life income situation where the beneficiary dies before many installments have been made.

Joint and Last Survivor Options. Joint and last survivor options are frequently used to pay endowment policy proceeds. The insured, and perhaps a spous or other party, are designated beneficiaries and are entitled jointly to the income while both are living with the payments to continue to the survivor on either's death. (Remember, endowment policies, although they have cash build-up, are for a period of time only and not the whole life of the insured.)

OTHER ALTERNATIVES

It is possible to receive the proceeds of an insurance policy other than immediately or throughout one's life:

As a Savings Account. Proceeds may be left with the insurance company with either a limited or unlimited right of withdrawal. The proceeds earn interest at an agreed upon rate with a guaranteed minimum.

Proceed to be Distributed over a Predetermined Period. Under this option the amount of each installment may vary according to fluctuating interest rates (generally with a minimum rate guaranteed) but the period of time over which payments are made is predetermined.

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Installment Amount Predetermined. This option states the amount of each installment is predetermined but just how long such payments will continue depends on fluctuating interest, as in the options mentioned above. The installments continue, anyway, until the entire proceeds are exhausted.

SUMMARY

Life insurance has many uses in addition to the protection it provides against the risk of premature death. The type of insurance that is right for you and how much you

should buy will depend upon your age and particular circumstances. You should seek professional help in designating your beneficiaries and in determining the amount of coverage you will need to buy presently in order to meet future needs. Be aware of the many settlement options open to you before deciding how the proceeds should be distributed if you are a beneficiary. consult the recommended reading list, especially to find additional information regarding social security. The worksheets will give you a better understanding of how your present coverage compares with your ideal coverage.

ONE WISH:

May you be lucky enough to find an insurance agent like the one who wrote a policy on a 97-year-old-man. When questioned by his superior the agent replied, "I checked with the computer and statistics show that few men die after age 97!"

Worksheet - Chapter 7

OTHER DEATH BENEFITS

1. Income producing assets that would be available to your family (heirs). Include separately owned, jointly owned and community property. Multiply by reasonable aftertax investment rate of return.

$_____

2. Property likely to be acquired by family from parents, others or trusts via inheritance or gift. (Estimate amount and give some idea of time period.)

$ _____

3. Other death benefits such as: social security survivorship benefits, annuities, non qualified deferred compensation plan, pension and profit-sharing plans, HR-10, IRA, TSA, or other employer sponsored plans.

$ _____

4. Total the face amounts of all life insurance listed on previous worksheet and subtract

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any outstanding loans that may be against them.

$ _____

5. Sum of all available death benefits = income available to family. (#1 thru #4 above)

$ _____

6. Compare estimated income available to family with "BUDGET"(found in Section Four Chapter 15 Worksheet) which you should modify to your own specifications. Take into consideration your own unique projections regarding the future inflation rate and any special medical or educational needs that you can foresee for your family.

$ _____

7. Is your family well provided for in the event of your premature death ?

_____

Do you need more life insurance or are you over insured?

_____

Recommended Reading
Chapter 7

How to Save a Fortune on Your Life Insurance, by Barry Kaye
The Life Insurance Conspiracy, by Spielmann & Zelman
Life Insurance: A Consumer's Handbook, by Joseph Belth
Life Insurance, from the Editors of Consumers Reports
How Your Life Insurance Policies Rob You, by Arthur Milton
Life Insurance: How to Get Your Money's Worth by Arnold Geier
Life Insurance: Theory and Practice, by Robert Mehr
Tax Facts on Life Insurance, by Samuel Scoville
How Life Insurance Companies Rob You and What You Can Do About it, by Walter Kenton Jr.

FOR INFORMATION ON SOCIAL SECURITY REFER TO THE READING LIST AT THE END OF CHAPTER SIXTEEN.

Chapter 8
Liability and Property Insurance

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Today, more than at any item in history, people tend to settle their disputes in court. We have been described as a nation of "Suers" (not "Sewers"). Awards to plaintiffs in recent years have been astronomical even when the defendant's liability has not been based on intentional wrongdoing or even negligence.

No matter how well a person has planned in all other areas of his life, if he has inadequate liability coverage he risks being wiped out financially by a single lawsuit.

DISCOVER YOUR RISKS

It is impossible to avoid all risk. Even if you were to stay in bed all day your dog might bite a passer-by; a tree might topple and destroy your garage or that of a neighbor; fire might break out in the basement, with or without any negligence on your part; a family member might be involved in an accident with your car; the postman might trip on the front stairs; your son might hit a baseball through old lady Fearful's window, causing her to have a heart attack, and so on indefinitely. From your bed you could find yourself involved in a myriad of lawsuits; some of them groundless! Like it or not, you would be stuck with the trouble and expense of defending yourself against these claims unless you had the foresight to acquire property and liability insurance in significant amounts.

RELEGATE VIA COST-BENEFIT ANALYSIS

The worksheets at the end of this chapter will aid you in discovering your risks and performing a cost benefit analysis. As we discussed earlier in Chapter 3, we have four alternatives in dealing with risk. (AART) Accept-- Avoid-- Reduce-- or Transfer the risk. In relegating each identifiable risk to its proper category, we must view it in the light of our overall financial picture. Since a home is often the major part of a family's net worth, the risk of destruction can neither be accepted or wholly avoided. Certainly by proper maintenance and good housekeeping (disposing of old rags and papers as a potential fire hazard for example) the risk of destruction to your home can be reduced. Almost universally, however, people would agree the risk must be transferred.

HOMEOWNERS POLICY

Homeowners policies are not just for home owners, there are special policies for tenants also. Besides insuring your home against things like fire, lightning and vandalism, personal property coverage is thrown-in and combined with the all important comprehensive personal liability coverage so necessary today. A homeowners policy is cheap when compared with the price of buying separately the three policies mentioned above.

There are seven common variations of homeowners policies. The recommended reading list will point you to information which will explain more thoroughly just how each policy differs. You and your agent, by taking into consideration your specific financial situation and exposure to risk, should be able to decide on a homeowners policy that is best for you.

CAVEAT (BEWARE)

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If you recall, both health and life insurance policies had 31-day grace periods in which your coverage continued even though the premium was late. There are no grace periods, as such, when speaking of liability and property insurance. When premiums are late you're not covered (unless another agreement can and should be worked out with your agent in advance).

CPL (Comprehensive Personal Liability Insurance) does pay property damage and for medical expenses incurred by a third party whether the insured is to blame or not. Of course there are certain legal technicalities; such as the determination of "trespasser statutes" and eliminating the possibility of their having been an intentional tort. However, the fact remains that benefits can be paid to a third party regardless of the insured's fault; something that is often overlooked by most people! Therefore any accident or injury should be reported if it occurred on your property or was caused by your self, family, employee or animal.

You should, of course, read your policy carefully paying particular attention to things that may suspend or reduce your coverage, such as leaving a property vacant over a specified length of time.

Although many of the exclusions found in " all risk" policies can be insured against with separate policies of their own, you should be aware of them. A few are: flood, earthquake, professional and business oriented liability, automobile, airplane and water craft liability and damage to property used by or rented to or under the custody of the insured.

AUTOMOBILE INSURANCE

An automobile is often the second most valuable property a family owns (home being first) and even more often it is the most dangerous. You may want to protect the value of your automobile for your own sake, but many states require you to carry insurance for the sake of others; to protect other people from possible damage inflicted via your car. Such coverage extends to liability arising from the ownership and the use of automobiles. Like the modern homeowners policy, there is a Personal Auto Policy which is more comprehensive in its coverage than the earlier auto policies were. Be aware of the areas excluded from coverage when you buy your policy. Nowhere does it pay more to shop than when purchasing auto insurance! Although price is probably your main consideration do not overlook the service record of your particular agent, the financial strength of the insuring company and the dividends certain companies may pay.

DEDUCTIBLES

Everything that has previously been said regarding deductibles when discussing other kinds of insurance, applies to property and liability policies also. It cannot be overemphasized that the higher your deductible the more coverage you can afford. You should pay (and therefore budget for it) repair bills under $200 or $300 yourself. That is not the job insurance was meant to do. Protection against catastrophe is what you need and should try and obtain in the most economical manner. Typically a premium increases of $10 or $20 can double or triple your liability coverage. Where else can you find such a bargain?!

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UMBRELLA CONTRACTS
OR EXCESS LIABILITY POLICIES

Umbrella contracts are insurance policies which appeared in recent years in response to the "million dollar plus" awards in liability cases. There is a required minimum limit of underlying liability in areas where coverage is available. The umbrella policy only provides for defense and pays liability claims after the limits of underlying liability policies have been exhausted. For example, if you have auto liability coverage with a $500,000 limit and the court awards Mrs. Maine, a passenger in the car which collided with yours, $1,000,000, the umbrella policy would pay the additional $500,000 beyond your auto policy limit for which your otherwise would be personally labile. Of course, the underlying limit requirements might be less than you are presently carrying on some of your policies. Check your limits on auto, water and air craft, CPL, professional policies and any others you may have. If you are able to reduce the underlying coverage to the point where your umbrella policy can take over, you will save premium dollars on these underlying policies!

Extended coverage is available that normally exists only as part of the umbrella (no underlying policy required). Included here would be protection form personal injury claims, (usually found only in business or professional liability policies) such as coverage for proof of (or in defense of) false arrest, invasion of privacy, wrongful entry, false imprisonment, libel and slander. If you have no underlying policies in these areas then you must pay a deductible which can range anywhere form $200/$300 to $1,000 or more depending on the coverage you seek.

Even if you think the chance of being involved in a lawsuit is small, the premiums are about the only thing I can think of that stand between you and potential financial disaster if you run up against one of Melvin Belli's colleagues in a courtroom.

SUMMARY

This chapter can briefly be summed up using the mnemonic DRIER

D - discover your risks
R - relegate those risks by use of AART (either Accept, Avoid, Retain or Transfer)
I - insure wisely (employ a cost-benefit analysis using deductibles)
E - evaluate your insurer. Comparison shop, checking financial soundness, and service as well as cost.
R - review periodically; your insurance coverage can quickly become outdated.

Worksheet - Chapter 8

WHAT IS YOUR PRESENT EXPOSURE
HOW MUCH LIABILITY CAN YOU HANDLE?

In your own notebook, answer the following questions:

1. Are you an employer, director or officer in a corporation or any organization?

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2. Is there usual exposure due to your profession, business or personal activities?

3. Do you own or rent any real property, automobiles, airplanes or watercraft?

4. Make an inventory list of your personal property. Include a brief description, purchase price and date of purchase or when it was fist acquired. Keep this in a safety deposit box.

5. Perform a cost-benefit analysis of your present property and liability coverage. Carefully compare the premium price with the coverage provided. Be aware of exclusion and non-responsibility clauses. Are you making the best possible use of deductibles? Are you over or under insured?

Recommended Reading
Chapter 8

You can Save a Bundle on Your Car Insurance, by Paul Majka
So you Think You're Covered, by Stanley Leinwoll
No Fault, by Paul Gillespie & Miriam Klipper

Section Three
Capital Accumulation

Chapter 9
Meet "SYDL P. TACCFL"

"Sydl P. Taccfl" is a mnemonic useful for analyzing investment proposals. In this chapter, we will proceed to discuss the relevance to your particular situation of each investment feature signified by the letters comprising "Sydl P. Taccfl's" name.

SECURITY.

HOW SECURE IS THIS INVESTMENT?

All of us would like to be able to get our money back in case something goes wrong in an investment. This is another area where you must allocate risk. (You should be getting to be an expert at risk allocation!) Depending on your age, temperament and goals, you must be able to look at an investment and decide if it fits within the parameters of your personal " acceptable risk" situation. If accumulating dollars quickly is your main motivation, then of course your risk tolerance will be higher than someone older, perhaps with more responsibility, who neither wants to nor can afford to lose what he already has acquired. Each person looks at a potential investment from his own unique perspective and with different expectations. Promises are seldom guaranteed and expectations may be disappointed. Can you accept the promise of higher interest from a corporate bond versus the increased safety but lower yield of a government backed bond? What if the corporate bond (bond issued by a private company) can't keep its promises to pay interest when due and principal at maturity? Or suppose you are considering

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investing in the stock market. Will the stock go up as you anticipate and will the company continue to make dividend payments as large or larger than in the past? The management and performance of the subject company is important, but it is not the whole story. Profits are dependent on a combination of many things: the economy, world wide as well as national, the overall health of all companies engaged in the same sort of activity as the one you chose; strikes; possible shortages of raw materials because of wars somewhere in the word; newly enacted legislation; higher interest rates; inflation, all can have unanticipated effects on your stock. A problem you will encounter in your security analysis is that often low financial risk goes hand in hand with high money rate risk. For instance, a bond issued by a financially sound company because of its high degree of safety pays only moderate to low interest rates; its safety is what attracts investors. However, when interest rates rise, these bonds, with their comparably low returns, decline in value in the market place. If you should need your money in any emergency you would have to take a discount on the bond; possibly less than what you originally paid and certainly less than you anticipated receiving had you been able to hold it to maturity. Because high interest rates intervened, your " secure" investment became a lose! This will be more thoroughly explained in Chapter 13 -- BONDS.

YIELD OR RATE OF RETURN

This section is entitled "Capital Accumulation." Capital accumulation could be defined in numerous ways but I choose to define it as the maximum return on an investment consistent with your already defined goals. Yield really determines just how much capital you can accumulate over a period of years. The "current yield" of an investment is the amount of income it yields annually compared to its current market value. The income may be in the form of rents, dividends, interest, appreciation (capital gains) or a combination of these. For example: a rental property that has a market value of $100,000 and brings in rents of $10,000/ year has a current yield of 10%. If the property was purchased for $100,000 and sold at the end of one year for $110,000 at the end of that year there would be, in addition to the 10% yield from rental income, a 10% capital gains also. Of course, this simplistic example assumes an all cash transaction which is indeed a fairy tale world. In reality the investment might have been made with $20,000 down payment, $80,000 mortgage and an additional expenditure of $15,000 for mortgage payments and a property "face life." In such a situation you'd have $120,000 on the plus side, consisting of the new property value of $110,000 and $10,000 rental income. The minus side would total $35,000 including the down payment, face left and a few mortgage payments. $120,000 subtract $35,000 equals $85,000, more than enough to take care of the mortgage. The mortgage is still $80,000 because payments were "interest only" meaning no reduction of the principal took place In this situation you would have made $5,000 on a $35,000 investment which works out to a 14% yield (not taking into consideration things like interest, depreciation and taxes which would increase your actual yield). It should be noted, however, that the property would have had to be kept at least a year and a day in order to be eligible for the lower capital gains tax treatment which is definitely worth postponing the sale for. Instead of being taxed on the entire $5,000 you made on this one investment, you would be taxed on only $2,000 which amounts to 40% of the whole gain. A more detailed discussion of capital gains and after-tax yields can be found in Section Five-- Taxation. In the chapter in this section dealing with stocks and bonds we will discuss coupon rates and yields to maturity.

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DIVERSIFICATION: HOW IMPORTANT IS IT?

Invariably financial planners urge you to diversify. Long before you ever heard of a financial planner you probably heard the old adage and have perhaps repeated it yourself: " Never put all your eggs in one basket." Andrew Carnage, the colorful oil tycoon at the turn of the century, gave the opposite advice: "Put all your eggs in one basket then watch them like a hawk!' His idea was you could never become rich unless you concentrated your powers: your effort, knowledge and dollars. A loose modern translation of his philosophy might be, " Go for it!!" I would agree with Mr. Carnegie that diversification is a defensive tactic-- a hedge-- and not a way to get rich quickly. On the other hand, getting rich quickly is not the investment goal of most people. many prefer a slower, steadier build-up of assets. To concentrate investments in one area, you must be prepared for possible large losses. Great gains are the reward of great risks. If you have determined you can afford to and want to assume those risks them diversification may not be as important for you and you can skim this discussion. It is important to remember Andrew Carnegie was a successful entrepreneur, not a financial planner. The reason for diversification seem quite obvious and make it unnecessary to go into in great detail. I'll enumerate briefly some of the advantages of diversification. High interest rates are great for new bond issues, hard on old, and tend to devastate real estate and dampen business expansion. hard assets, such as precious metals, art, diamonds and collectibles, respond to bad news by rising in value, whereas the value of stock falls. Real estate is seen as a hedge against inflation and as such would counter the loss of purchasing power that would occur when dollars are invested at a fixed rate of interest over more than a few months. In uncertain markets, such as we've encountered in the 80s, I would especially concentrate on diversifying the time when investments mature,. In general, try to keep investment cycles short so that dollars are not tied up for long periods at what may ultimately proof to be a non-competitive interest rate. Short term investments are best in a fluctuating market. Stocks rise in a booming ("bull") market. This expansion so beneficial to stock holders in general, depresses the bond market. Money is sought by expanding companies in "good times." Too much demand results in a shortage which pushes interest rates higher. Bonds bearing lower interest rates than are currently being offered must be discounted. This phenomena was mentioned when "Security" was discussed earlier. Although neither bonds nor stocks as a class, are absolutely secure, diversification prevents big losses. As you can see, if you owned both typed of investments, a "wash" rather than a "swamp" would occur if the market fluctuated suddenly and wildly.

LIQUIDITY

I prefer the definition of liquidity found in Sylvia Porter's *Money Book* (which, if you don't own, you should rush out and buy a copy immediately. If you only buy one book out of all the ones I recommended let it be Sylvia Porter's. It is a quick, easy reference to almost everything financial and you will find yourself referring to it often.)

> "LIQUIDITY: Capacity of the market in a particular security to absorb a reasonable amount of buying or selling at reasonably limited price changes. An "illiquid" market in a security means you cannot buy or sell with reasonable freedom at reasonable price changes."

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A shorter definition might be to say that, "Liquidity is cash or cash equivalents." Up until recently you were penalized for keeping dollars in Savings and Loans and Banks where the rate of interest paid was far below inflation rates. Your dollar was " shrinking" even as it provided a ready emergency fund for you and your family. That drawback has generally been eliminated with recent legislation allowing these institutions to offer competitive interest rates on the money deposited with them. Rates and regulations concerning withdrawal penalties vary from institution to institution so check these provisions carefully. Planners used to advise clients to keep anywhere from three to six months' wages on hand for emergencies. An argument against this practice is that it is just plain "stupid" to have money lying around not working for you. It should be gathering interest, expanding and perpetuating itself. After all, how many times does an emergency occur that cannot be handled without cash? Now as I pointed out, the question is almost moot, because the interest banks currently pay is comparable to that paid by many less liquid investments. Presently, the key seems to be whatever makes you feel comfortable is the amount you should keep in liquid assets. Liquid assets commonly include checking and saving accounts, money market funds, U.S. Government Savings Bonds, brokerage accounts and cash values on life insurance policies.

PROTECTION FROM CREDITORS

Actually there are no investments which, standing alone, would be beyond the right of your creditors should you ever get into financial difficulty. However, you should consider the possibility that a creditor might at some time in the future have reason to attempt to try and get at your assets and that possibility should be dealt with when your purchase of a new investment is made. The manner in which you take title to the investment can perhaps shield it from creditors. The whole broad, and often overlooked and little understood, topic I am referring to is *trusts*. Very little use is made of trusts by the general public. They are unfortunately and erroneously seen as being the domain of the super rich. Actually a trust may be very simple or quite complex depending on your wishes. It is merely an agreement whereby you give property to a third party (trustee) who is expected to mange and invest it for your benefit or the benefit of whomever you choose (beneficiaries). The property is not owned by you, it is owned by the trust, with the trustee being liable for debts against the trust as a separate entity distinct from you personally. I would advise you to look into the use of trusts in your overall estate planning. They have a variety of uses which I will go into in greater detail in Chapter 23. Just in passing I might mention that spendthrift clauses, which may be put into life insurance settlement options, also are used to protect investments form creditors. The laws vary from state to state. Usually an installment option must be chosen and only the proceeds held by the insurance company are protected from the claims of the creditors. In other words, the creditors can only get at the proceeds after they are distributed to the debtor (out of the insurer's control).

TAX IMPLICATIONS

Since an entire section of this book is devoted to the role taxes play in your financial planning, I will be brief here. You should be aware that some investments are tax free, others are tax deferred and still others taxed at capital gains rates. Therefore, in comparing yields, do not fall into the trap of comparing "apples and oranges"; i.e. equating a 9% return form a tax-free bond with a 9% return from one that is taxed at ordinary income rates. I like to think of "Tax

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Implications" as being analogous to the "Magic Wand" that transformed a plain pumpkin into Cinderella's Coach. These almost magical investments are called Tax Shelters. Their glamour is not so much in the return they promise but in their ability to shield other dollars from the tax collector. They accomplish this feat by the use of depreciation, other deductions and various credits which will be discussed more thoroughly in Section Five.

AMOUNT NEEDED

It is obvious that you cannot choose any investment you like solely in terms of safety, yield, diversification, liquidity and tax implications. You are restricted to the amount available to you for investment as well as the demands of the investment. Of course, "available to you" does not necessarily mean just what is squeezed out of the family budget at the end of the month. You've heard: "Where there's a will there's a way." If you discover a bargain investment it is not only possible but probable you can "find" the dollars needed. A commercial or private lender could be convinced to put up the required capital and split the potential profits with you.

I recognize that people are not comfortable with "aggressive investments." If you have the temperament, interest and the goal of becoming "wealthy" rather than just secure , then the amount needed should not curtail your investment possibilities but only be viewed as another piece of information in your overall analysis. Always remember you can do whatever you truly want to do! There are many excellent books to help and inspire you listed at the end of this chapter and at the end of Section One.

COLLATERAL

Collateral is anything of value that you offer to a lender for security for a loan. If you are unable to pay back the loan for any reason he can liquidate the collateral. He would be entitled to cash proceeds up to the amount of the loan and you would be entitled to any amount remaining above that figure. Not all types of investments can serve as collateral for a loan. Some of the best collateral are savings accounts, cash value of life insurance policies, good quality securities, equity in home or automobile and other improved property. These are all things you don't want to liquidate either because you are currently enjoying their use or getting good returns which you don't want to give up in a scale in order to go into another investment. Usually when you offer collateral for a loan it is a case of wanting to have your cake and eat it, too, and it is possible in the world of finance! You don't want to take out the cash you have in savings and perhaps suffer a penalty and give up the interest it is making buy you do want to purchase something else. Because you have the power to pay for it (if you wanted to) as evidenced by the collateral, you are given the money to do so (loan). What's the old saying: "Them that has gets," or the talk about "the only time you can be certain of getting a loan is when you don't need one."

Highly speculative investments do not make good collateral. It is not uncommon when shares of a volatile company are pledged for a loan and the stock market dips too far to find the lender forcing the shareholder to sell at an unfavorable price in order to keep his loan out of jeopardy. The same thing happened to people who had gold as collateral for loans. When the gold market collapsed from highs of 800, many people were forced to sell at a loss to cover their outstanding

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loans. Where you, as an investor, might choose to "ride out" a bad market hoping for the value to return, a lender will not allow you to do so.

Whether or not an investment is suitable as collateral is only one more piece of information to evaluate when considering what type of investments you want to own. As you can imagine it only has relevance when almost everything else is equal.

CALLABILITY

When buying stocks and bonds check to see if there is a call provision; if so you might want to shy away from this offering. A call provision is the right the issuing company reserves to pay off obligations before maturity; generally subject to enumerated conditions.

When you look at the money you have before you to invest (forget for the time being any talk about promoting bargain investments) and divide it up to achieve your goals after some very careful and time-consuming thought, you don't want to have your plans upset by a company redeeming your stocks or bonds when it suits them and not you!

Many corporate bonds and most issues of preferred stock are callable. Companies naturally would like to redeem their obligations when interest rates decline below the level at which they were sold. The idea is to replace them with new issues bearing lower rates. Your desire is to keep the higher return which is probably the reason you were attracted to the issue in the first place So you will not find yourself at cross purposes with a corporation you should check carefully when considering the purchase to see if there is some protection against a call for at least a certain period of time and with a limit to the price at which it may be called.

FREEDOM FROM WORRY

You almost subconsciously take your own temperament and attitudes into consideration when choosing an investment vehicle. I want you to do it consciously! The worksheets in Section One should have made you more aware of your strengths and weaknesses; whether you are a risk taker or need security; whether you would prefer to take an active or passive role in your investments; whether your goal is to be a millionaire of just to live comfortably. Now its the time to be cognizant of all these things and eliminate some investment possibilities from your consideration.

Freedom from worry means different things to different people. Some people find they are, and prefer to remain so wrapped up in their careers that they don't have time to bother with investment decisions. For them, mutual funds might be a natural selection. Other people find they get very nervous if they are even a little bit in debt-- they should definitely stay away from aggressive investments where they may be liable for large amounts of money (tied up) at certain times during a transaction. Maybe you can't stand the "ups and down" of the stock market; on the other hand perhaps your job is sometimes experience from the stock market may be exactly what you crave! If you are good with your hands and like to design things, enjoy working with people and love to speculate, buying rundown properties, fixing, and renting them may be your perfect investment vehicle. However, if you prefer to take a passive role don't rule real estate out

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because you can still share in the fever of speculation without investing time or labor. Contributing investment dollars as a limited partner might be something you should look into.

Bernard Baruch once said in reference to the stock market, but it holds good for anyone trying to find his own particular investments threshold, "Sell until you can sleep at night." You may be sorry if you fail to hold your potential investment up to the scrutiny of this feature of SYDL P. TACCLF!

LEGALITY

We can all think of 100 ways to get rich quick-- but are they legal? In most case, the answer is obvious! this feature is included here to remind you to check very carefully before proceeding in those cases that are not so obvious; the gray borderline investments that sound too good to be true just may not be honest! If you have your suspicions don't let greed make you throw discretion to the wind. A new scheme is born every minute; and a sucker to go with it. Tax shelters are especially vulnerable. Also the many ways to keep your money free from taxes by using offshore trusts need special scrutiny. Many people who "get caught" are not crooks, they're just gullible and want to believe in the good fairy ! Don't neglect this all important area when analyzing your potential investments.

Recommended Reading
Chapter Nine

Complete Money Market Guide, by William Donoghue
The Smart Investor's Guide to the Money Market, by Paul Sarnoff
Your Book of Financial Planning, edited by Loren Dunton
The Intelligent Investor, by Benjamin Graham
How to Live with Your Investments, by Linhart Stearns
How to Read the Financial News, by Norman Stabler
Financial Planning Handbook, by Harold Gourgues
Personal Financial Planning, by Hallman & Rosenbloom,
Institutional Investing, by Claude Ellis
Papermoney and Supermoney, by Adam Smith
The Battle for Financial Security, by Roger Birdwell
The Alpha Strategy, by John Pugsley
Is Inflation Ending? Are You Ready? by A. Gary Schilling and Kiril Sokkoloff
Wealth Magazine

Chapter 10

Common Stock

Common stock is tangible evidence of an equity ownership in a company. A stockholder shares in the successes and risks of an enterprise. When a company is not doing well, the price of the stock declines. When the company is making a profit, each share increases in value, i.e. the price

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of the stock goes up. Usually part of a company's earnings are distributed to the stockholders in the form of dividends, the remainder is used for business expenses and expansion. The amount to be distributed and when, are decisions made by the board of directors elected by the shareholders.

HOW TO DETERMINE THE WORTH OF A PARTICULAR STOCK

The price of one share of a particular stock which is traded on the New York or American Stock Exchange (and these are really the only stocks a novice should concern himself with) is quoted in the financial sections of most local newspapers.

To find the "worth" of a stock takes a little more effort! Companies send annual reports to each stockholder. Almost half of these "owners' throw the reports away without even opening them.

"Don't! The Annual Report is the key to determining the current health and direction your company is headed. Look at the ten year summary; have earnings been increasing or decreasing? How much has been invested in upgrading, inventory and new innovations? These answers will help determine your company's potential for future profits.

The market price of a conservative stock tends to keep pace with its earnings per share. The earnings per share are computed by subtracting any preferred dividends from the company's net profits and dividing the remainder by the number of shares outstanding. The earnings per share is useful by itself and also necessary to compute the price earnings ration (P/E).

The P/E ratio of a stock is the market price divided by the most recent per share earnings. If the Widget Company sold for $50/share and its per share earnings were $5, its P/E ratio would be 10. (50 dividend by 5). That means it takes $10 of market value to purchase $5 of earnings!

There are two other commonly used indicators of a stock's worth. One is the "yield" meaning the percentage that the dividend bears to the market price of the stock. For example, getting back to the Widget Company, whose stock is selling at $50/ share and pays a dividend of $3 on each share, the yield is 6%. (3 divided by 50) For the yield to have any meaning to you, you would have to know the normal yield in the industry and not only how the Widget Company's yield compared to similar companies but also to its own record over the years.

The "book value" is also an indication of a stock's worth. The book value has nothing to do with market value. It is simply a company's net worth (assets minus liabilities) minus the liquidating value of any preferred stock. To find the book value per share just divide the number of outstanding common shares. This does not tell you much about the potential of a company; it really says nothing about the projected earnings or expectations of the company for the future. What book value does do, is tell you the liquidating price. It establishes the bottom line. A company, even with a poor earnings potential , would not anticipate its stock falling below book value.

STOCK SPLIT

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When the price of a stock gets too high a company often divides the number of outstanding shares. In a two for one split a stockholder with 100 shares at $80/share will now own 200 shares at $40/share. The hope is that more investors will be encouraged to buy the lower priced offering. You can see the stockholders value is not increased by the split, as such (100 times 80 and 200 times 40 both = $8,000) but increased activity may drive the price up. Psychologically it looks like a better deal to buy at the lower price. Who would you say is getting the better deal, the guy who buys a double ice cream cone for $1.00 or two singles for $.50 each? It might depend on whether he has two hungry kindergartners or is a teenager with a load of books. You can see, however, the market value of the ice cream is the same.

KINDS OF COMMON STOCK

SPECULATIVE

In a sense all stock is speculative because the profit is unknown; not "built in" like it is with bonds. You know if you buy a bond at a certain price and hold it for a certain period of time (maturity) you will have X dollars; that is if the corporation is still in existence and financially sound when the time comes to redeem it. The only thing that is really uncertain (speculative) about a bond is the price you can buy or sell it for before maturity. This unknown price is referred to as the discount (if lower) or premium (if higher) bond price. As the term is used in reference to the market, speculative stocks are new issues, glamour stocks, penny stocks or any stock usually low priced because it is unproven. These stocks often rise and fall in price quickly and drastically as compared to the rest of the market.

GROWTH STOCK

Growth stock usually appears to be expanding its profits ahead of the market and general economy. The P/E ratio may be smaller than that of the purely speculative stocks but it is greater than the more conservative. Growth stock may be the proper investment vehicle for people fooling for relatively fast capital accumulation but who are not willing to accept as much risk as demanded by the more speculative issues. As is true of speculative stock, the price here is an anticipation of future profits rather than an indication of current earnings.

CONSERVATIVE STOCK

The stock with the longest history of weathering the market's ups and downs and paying dividends through it all , are called "blue chips". Blue chip companies are usually old, established firms with records showing consistent, though not necessarily spectacular, profits over the years. Dependability and income from dividends are characteristics of these stocks. Their P/E ratio is more conservative than that of the speculative and growth stocks. The earnings tend to justify the price. This is the ultimate in safety for those who desire stock in their investment portfolios.

CYCLICAL AND DEFENSIVE STOCK

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Certain companies are dependent on the business cycle to a much greater degree than others. Because they are manipulated by forces economic and political, beyond the control of the company, the stock tends to fluctuate wildly. Examples of cyclical stock that a few years ago suffered devastating declines are the aerospace and auto industry issues. On the other hand there are the so-called defensive stocks which fluctuate very little. Usually these stable companies provide necessities of life such as food and utilities.

OVERLAP

It is not surprising that a blue chip or defensive stock can also be considered a growth stock or income stock. A stock that starts out speculative (as most do) can wind up a few years later qualifying for the growth or conservative category. If it continues in existence long enough, showing consistent profits and dividends, it may wind up a blue chip! Unfortunately the opposite can also occur. GM for years was considered a blue chip company but in the 80s it would be more realistically classified as a cyclical stock.

HOW TO BUY STOCK

DOLLAR COST AVERAGING

Dollar cost averaging might be called "time diversification." It is a plan whereby you, as an investor, commit yourself to investing a specified amount of money at regular intervals over a long period of time without regard to the short term swings of the market. For example if you put $59/month into the *Widget Company* over ten years, you would find some months your $50 would buy more stock (lower priced) than others (higher priced). At the end of ten years you would have acquired a large chunk of Widget Stock at a very good price.

Remember this is not a foolproof way to buy stock. The *Widget Company* may not justify the faith (and dollars) you put into it. Its market price, which under this system you try so hard to ignore on a day-to-day basis, could conceivably be on a one way track; down only!

Just as unlikely but still to be considered is the fact that, due to some emergency, you might have to sell when the market is at a low. The whole purpose of this book is to help you avoid such a possibility. If you have read this far you would not find yourself in such a precarious situation because you would have adequate insurance for such an emergency situation, other liquid assets and would not be using dollars you could not afford to lose in the first place!

EMPLOYEE SAVINGS PLAN

A relatively painless way to practice dollar cost averaging is through an employee savings plan. If there is one where you work you may find your employer will put up either a matching sum or other amount for each dollar of your wages you set aside for investment. The investment money is automatically deducted from your paycheck. Together with the employer's contribution it is put in a trust fund set up for this purpose. Sometimes the savings are used to purchase the stock of your employer's company but more often they are invested in several stocks (mutual finds) and professionally managed.

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If you have the option of reinvesting your dividends I would recommend you do so. You will get compounding not only on interest over the years but will have another way to acquire additional shares. Sometimes if a bank is involved, there is a small fee. If the reinvestment program is handled within your company there is usually no charge involved. Check with your employer to see if you qualify and to get the details on the plans available to you.

INVESTMENT CLUBS

Social investment clubs were around before the turn of the century. In 1951 they were formally launched with an education objective. The address of the National Association of Investment Clubs is listed at the end of this chapter They provide instructional material and aids at a nominal cost for those people serious about accumulating capital in a conservative supportive environment. If you want to "Do it Yourself" (investing) be sure to write for their handbook.

INVESTMENT COUNSELORS AND BROKERAGE HOUSES

Many people open individual accounts with a brokerage house. If you are a novice it is best to choose one of the larger famous houses with a sound reputation. Choose your individual broker as you would your doctor, auto mechanic or attorney. Find one whose expertise is in your area of interest. You don't want a broker whose specialty is venture capital when you are looking for income stock. It helps if his philosophy is similar to yours and that you feel comfortable also. This is essential if you intend to give him discretion over your portfolio (i.e. all your investment holdings) via a limited power of attorney. A limited power of attorney would allow the counselor to do certain specified things on your behalf. You in effect give your permission for him to buy and sell, using his own judgment as to price, time and amounts, all within whatever limits you choose to set. You would in such a case, be hiring an investment counselor, who for a fee (usually a percentage of your account, paid annually), would treat your investments as if they were his own. If you profit overall he will too; remember his is a percentage fee. However, it is hard for me to advise anyone to go this route because it is obvious who will lose the most if he mishandles your account! I think anyone who would want to put his investments blindly into the hands of another would not be reading this book so probably a caution is not necessary. If I am wrong and there is a reader out there thinking of hiring a discretionary investment advisor, I cannot overemphasize how important it is to get as many references as possible both from financial institutions and clients of the proposed advisor. Make certain he has adequate liability insurance and an impeccable reputation. Brokerage commissions are paid in addition to his advisory fees and usually to your own or another broker (of the advisor's choosing).

If you are planning to act as your own counselor and only intend to pay a broker's commission on the orders executed at your direction, then trust is not quite so important and may even lull you into a lazy dependency once you develop it! Many brokers are quite knowledgeable and should be relied on for advise but usually in answer to specific questions. These houses figure a certain amount of counseling into their brokerage fees. There are discount houses which charge smaller fees but do not make recommendations or otherwise advise you regarding a transaction; their only function is to execute your orders. Again a word of caution: only the most knowledgeable and sophisticated investors would benefit from the savings. The advice you as a novice could otherwise receive from a broker is worth far more than any savings you might

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imagine you would realize by using a discount house. As you will discover in chapter twelve, I think mutual funds are the ideal solution; a happy medium to this problem. Besides paying less for advice than you would pay a discretionary counselor, you are free to accept or reject it according to your own judgment.

WHEN TO SELL

The most obvious reason for selling your stock is the need for money.

Another happier reason for selling is the desire to take a profit before the stock takes a downward slip and wipes the profit out.

A third reason is to get out of a bad deal. Maybe your stock is going down or has stood still over too long a period of time.

A final reason to sell is to make what you hope will be a profitable switch. Perhaps you see a chance to get a higher return on your investment dollar by selling the current stock and investing elsewhere.

One word of caution; in all instances it will be to your advantage to have held the stock at least one year before selling. That way you are taxed at capital gain rates. We will discuss capital gains more thoroughly in Section Five, but roughly it means you will be taxed on only 40% of any income resulting from investments held more than a year.

INDIVIDUAL INVESTORS INCENTIVE ACT

H.R.63 was introduced to Congress by Representative Richard Schulze of Pennsylvania in 1983. Briefly the Act allows for a 10% tax credit , up to $1,000 for individuals and $2,000 for couples, for the purchase of stocks, bonds and mutual funds that invest in American corporations. If passed it will make stock ownership more attractive to thousands of Americans and will thereby provide needed capital to industry and small businesses. New capital means modernization, innovations and jobs. However, the nation's huge budget deficit has made it extremely difficult for any legislation proposing either an increase in funding or, as in this case, a restriction on revenue, to gain acceptance by Congress. This appears to be a very unfortunate and shortsighted attitude because modernization and new jobs means more revenue for the government.

SUMMARY

Try and buy the strongest stocks in the strongest groups. Choosing the best group of stocks to invest in at any given time is harder and infinitely more important than choosing the highest flyer in that group. Do not enter the market at all unless you can take losses is your stride. A certain amount of losses are certain to occur. It is hard to find the right point between diversification and concentration. Too little diversification is risky but too much prevents your making any meaningful profits because if you hit a real winner you will have so little invested it won't do much for you.

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George Santayana said, "Those who cannot remember the past are condemned to repeat it." History is really a preface of what is to come. That's why it is so important to study the history of an industry and the past record of a corporation before you invest your money. From this study a well-considered expectation of the future should emerge and that in the end should determine your investment decisions.

Again I draw your attention to the worksheet and recommended reading list at the end of this chapter.

Worksheet - Chapter 10

COMMON STOCK
ARE STOCKS A PROPER INVESTMENT MEDIA FOR YOU?

1. Can you accept risk? Financially? Emotionally?

2. What is your specific investment goal? Check one.

_____ long term growth?
_____ current income?
_____ security of principal?
_____ other?

3. Do you have time to inform yourself about a company?

4. Have you checked your broker's references even if he is a member of a well-known large and reputable firm?

5. Have you investigated dollar cost averaging?

6. Do you have the courage to cut your losses short and not keep hoping for an "upturn" in the market?

7. Do you have an overall plan for investing and can you stick to it?

8. Do you have the patience to wait for a stock to move, not expecting too much too soon?

9. Do you have the discipline to refuse to act on rumor or a "hot tip"?

ANALYZING A PARTIUCLAR STOCK

1. What is the P/E ratio of this stock?

2. Is it higher or lower than the P/E of its competitors?

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3. How is this company ranked compared to the industry as a whole? Which range --TOP--MIDDLE--BOTTOM--

4. Is this an improvement, decline or the same as one year ago? Five years ago?

5. What do you know about the present management?

6. Is this company diversified or is it dependent on only one product or service for its profits?

7. Is the company in a growth industry?

8. How great and how consistent is the demand for the company's service or product?

9. How will new technology affect this industry?

10. Is the overall industry stable or subject to roller coaster type movements?

11. Is the industry dependent on imported raw materials or labor?

12. How are labor relations within this particular industry? Have you considered the likelihood of strikes?

13. Has there been recent upgrading in the company in terms of plant, inventory or other innovations?

14. What is the book value of this company?

15. Is this year's yield better than in former years? Is the yield of this company normal for the industry?

16. Would you classify this stock as GROWTH? SPECULATIVE? BLUE CHIP? CYCLICAL? CONSERVATIVE? DEFENSIVE?

Recommended Reading
Chapter 10

Stock Market Primer, by Claude Rosenberg, Jr.
Investing on Your Own, by Richard Thorsell
How to Make $1,000,000 in the Stoock Market Automatically, by Robert Lichello
Reality in the Stock Market, by Roger Birdwell
Odds on Investing, by Brody & Bliss
Heads You Win, Tails You Win, by Ray Dirks
Get Rich on the Obvious, by Tom Taylor
How I Made $2,000,000 in the Stock Market, by Nicholas Darvas
How to Profit form the Coming Bull Market, by Max Ansbacher
How to Make Money in Wall Street, by Louis Rukeyser

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The Downbeaters: How to Buy Stocks That Go Up, by Gobleigh & Dorfman
Dow 3000, by Thomas Blamer & Richard Schulman
Valuing Common Stock, by George Lasry
The Dow-Jones Irwin Guide to Common Stocks, by Moder & Hagin
How to Select Undervalued Stocks, by Robert & Darryl Peisner
How to Select Rapid Growth Stocks, by Robert Peisner
The Stock Market: Theories & Evidence, by Lorie & Hamilton
The Stock Market Handbook, edited by Zarb & Kerekes

For information on investment clubs write:

National Association of Investment Clubs
1515 E. Eleven Mile Road
Royal Oak, MI 48067

Phone: 313-543-0612

Chapter 11

BONDS

A bond is a promise to pay interest at a fixed rate (coupon rate) and to redeem the promise at a predetermined time for more money than the consumer paid when he first bought it. Because there is no uncertainty as to the amount of interest income one might expect form a bond and the redemption price is set before the initial purchase, a bond is referred to as a fixed income investment. As was mentioned briefly in the last chapter, the main risk as to what your bond will be worth at maturity or what income you can expect from it has to do with the financial stability of the issuing entity. Stocks and bonds share this uncertainty. The ability of the issuer of both to meet its obligations in the future is unknown and at the risk varies from one entity to another.

CONTRASTED WITH STOCK

If you buy stock you become an owner and expect to share in the company profits. If you buy bonds, however, you become a lender and expect a fixed amount of interest. After the second world war yield on stocks was double that of bonds. In the 1970s that situation was reversed. Thanks to compounding high interest rates investments in bonds often doubled in nine or teen years. Compounding meant that an investor received interest, not only on the principal amount invested, or in the case of bonds, the face value of the bond buy interest was paid on the accumulated interest each time also. Compounding is a bonanza for the investor! He receives interest on his interest. On top of everything else stocks have recently encountered tough competition from the bond market because bonds offer greater protection against wild or hostile economic conditions than do stocks.

YIELD

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A yield on stock, if you recall, was computed by dividing the dividend by the purchase price. Similarly, to determine the yield on bonds, divide the interest by the price you paid for the bond. For example: $1,000 bond pays 10%/year and you bought it for $900. Remember, interest is paid on the face value; therefore 10% of $1,000 is $100. The yield is 100 divided by 900 or approximately 11%. It should be noted that yield to a maturity would be higher because in addition to interest you would receive an extra $100 more than you paid for the bonds. Your broker can help you with this computation, or, if you like, there is a reference book (listed in the reading list at the end of this chapter) which has the computations already figured for you.

BOND RATINGS

All bonds are rated according to the credit worthiness of the issuing entity (borrower). The most secure are rated AAA down to AA, to A and on through BBB and CCC to the most risky grade, C. Along with yield and market price the rating is of prime importance when analyzing a potential investment in the bond market.

CALL PROVISIONS

Another consideration is the presence or absence of a call provision. We mentioned "Calls" earlier in Chapter Nine. To reiterate: you buy a bond with the idea of receiving a fixed interest income over a period of time. A call provision allows the issuer to call these bonds should interest rates decline below the levels at which they were sold and to replace them with new issues bearing lower rates. There are certain restriction such as the price at which the entity reserves the right to call in its bonds and the time which must elapse before a call is permitted. Often you can get a five-year protection against calls which would in effect guarantee the interest rate you "bought" for at least that period of time. Naturally, look for bonds without call provisions whenever possible.

DISTINGUISHING BETWEEN BEARER AND REGISTERED BONDS

Receiving interest on your bearer bonds is not the automatic operation you may be used to in your savings account. You must take an active role in obtaining it. A bearer bond is like cash and should be treated as such. If you lose it it's "finders keepers"; you have less proof of ownership than you do with a traveler's check. These bearer bonds have coupons attached to them which you must clip and redeem at a bank in order to receive your interest.

Registered bonds have your name on them and are registered with the issuer who sends you a check when the interest is due. This makes them not only safer but more convenient than bearer bonds.

HOW TO BUY BONDS

The face value of a bond is the amount the issuer will pay when the bond is redeemed at maturity. Bonds are sold at a percentage of their face value but interest is paid on the whole face value. A bond that is bought at a premium is bought for more than its face value. You might

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wonder why anyone would pay more for a bond currently than what he can get for it in the future. The attraction is the interest rate. A person buying a bond at a premium would be acting on a belief that interest will fall in the future. His aim would be to capture what he believes to be a high interest rate now.

Underwriters function as wholesalers between the borrowing institution and the investor (lender). They in effect, buy the bond issue from the borrowing entity at a certain figure and resale it to the individual investor at a higher price; the underwriters"' mark up".

It is possible to purchase from the Federal Reserve. There are also many bond funds available which are similar in concept to the stock oriented mutual funds. These bond funds are professionally managed and can consist of a variety or a selection of only one type of bond. The "all government" bond funds are popular because of the security they offer. Frequently bonds are chosen and put into a trust called a unit investment trust. The trustee, generally an investment banker or broker, then sells "units" in the trust to investors.

KINDS OF BONDS

There are three main kinds of bonds each having numerous sub classification. There are Corporate Bonds, Municipal Bonds and U.S. Government Bonds.

CORPORATE BONDS

Utilities are the largest issuers of corporate bonds, followed by private industry, finance companies and real estate organizations.

Mortgage Bonds. Mortgage bonds are bonds secured by a mortgage on all or a portion of the fixed property of the borrower. Utilities almost always issue mortgage bonds because the collateral offered (a lien against real assets) is a needed enticement to investors.

Debenture Bonds. Debenture bonds are unsecured. They do not offer collateral for their loans but only the credit of the issuing corporation. That means holders of debenture bonds are in line to be paid off after the secured lender (holders of mortgage bonds for instance). As their name implies, subordinated debentures are subordinated to senior debt and income debentures are only paid interest if and when it is earned. If the company experiences financial difficulty the interest my be accumulated slowly but must, at any rate, be paid to the income debenture bond holders before dividends are paid to any stockholders. Convertible bonds may, at the holder's option, be converted to stock; not as safe as bonds but more speculative and desirable under certain market conditions.

MUNICIPAL BONDS

Municipal bonds are issued by local and federal governments and secured in several ways. The highest security is offered by *General Obligation Bonds*. The "full faith and credit" of the borrower is hard to beat when that borrower has general unlimited taxing powers.

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Special and Limited Tax Bonds are backed only by a potion of that taxing power. Often the borrower is restricted to paying interest from only one special tax.

Revenue Bonds are paid from the proceeds of the self-supporting projects for which they were raised.

Because the federal government backs local Housing Bonds these bonds are among the most secure and are consequently awarded high ratings.

The most important and best publicized feature of Municipal Bonds is the fact that they are exempt from deferral and sometimes state and local taxation. When compared to the after-tax yield of other investments, municipal bonds can be quite attractive. We will discuss them again in Section Five as a vehicle for reducing taxes.

GOVERNMENT BONDS

U.S. Savings Bonds. Most of us are familiar with U.S. Savings Bonds. They have been a typical birthday or Christmas gift from a distant Aunt and Uncle. How many 13-year-olds have received savings bonds for their Bar Mitzvahs during the past 40 years? Savings Bonds are registered so the birthday child's name is place right on the security which makes it extra special! These bonds can not be "called" before maturity and are not transferable. I am describing E Bonds. Today Series EE are sold with a face-value of $25 up to $100,000. The maximum annual purchase allowed an individual is $10,000. The larger denominations are used to fund employee savings plans. EE Bonds don't pay interest as such, but since they are issued at a discount, the yield you get at maturity or whatever date you choose to redeem them (redeemable after two months) can be compared to interest. Of course the longer you hold the Bond the better your return.

Savings Bonds cannot be sold in the market place. Since they are non-transferable securities, they cannot be used as collateral for a loan but can only be redeemed by the government. There is no state or local tax on savings bonds and federal income tax is deferred on EE Bonds but not H Bonds until the bonds are redeemed. This is a useful and money saving feature which will be discussed in more detail in Section Five.

Series HH Bonds are sold at their face-value and pay interest twice a year. The lowest denomination is $500 and the maximum purchase allowed in one year, as in the EE Bonds, is $10,000. You must hold HH Bonds at least six months after the issue date before attempting to redeem them.

Treasury Bonds. These are backed by the United Stated Government and they make up most of the federal debt. They can be purchased in bearer or registered form. They are considered long term debt and generally take ten years to mature. Interest rates naturally change over a long period of time. When the rates offered in new issues is higher than what your earlier issued bond is paying the price of the earlier bond naturally declines; i.e. if you were to sell it before maturity. If you hold it until maturity it can be redeemed for face-value. However, the higher interest that you could have had from some other investments is still sacrificed.

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OTHER GOVERNMENT SECURITIES

U.S. TREASURY BILLS

U.S. Treasury Bills are sold at a discount and mature in three-six-nine- and twelve months. They don't pay interest but your "profit"(difference between what you paid for them and what they were redeemed for) is comparable to interest. They are issued only in bearer form with a minimum purchase of $10,000 required.

TREASURY NOTES

Treasury Notes are securities that pay interest every six months. Their maturity dates range form one to ten years. Here also there is a minimum purchase requirement of $10,000. You can buy government securities through your broker or bank. New issues can be bought directly from the Federal Reserve without service charges or commission. Because of the large amounts involved you can see that this action should be the domain of the sophisticated, knowledgeable investor. There are books listed at the end of the chapter that will satisfy your curiosity and with some study and continued effort government securities may be the ideal investment for you one day.

SUMMARY

Bonds are usually considered a safer investment, more conservative, than the stock market. A bond holder is a lender with fixed interest income rather than a partial owner facing future losses or profits. But bonds are not without their pitfalls. There are three main kinds of bonds: U.S. Government, Municipal and Corporate. The government bonds offer the greatest safety; the municipals are tax-exempt; and the corporate bonds offer the greatest monetary rewards. The two biggest enemies facing the bonds market are high inflation and high interest rates. It is conceivable that inflation could rise high enough to offset all growth. Thanks to inflation, the investor's purchasing power would be the same as the year the investment was made. During periods of high interest, prices of bonds issued during earlier lower interest years would be depressed. However, this in itself would not greatly affect the holder who could afford to keep the bond to maturity. On the other hand, those forced to sell earlier would have to suffer large discounts due to the high interest rates an investor could get form the new bond issues.

Worksheet - Chapter 11

A CHECKLIST FOR THOSE CONSIDERING THE BOND MARKET

1. Are safety and income your prime objectives?

2. How long do you want to leave your savings in a fixed-income medium?

3. Can you afford to take risks?

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4. What do you think the inflation rate will be in 2 years?
5 years? _____10 years $ _____20 years? _____

5. Will your interest coupons cover any annual loss of purchasing power your invested dollars may suffer if your inflation predictions are realized?

6. What do you think interest rates will be in 2 years?
5 years? _____ 10 years? _____ 20 years? _____

7. If your interest rate predictions come true and if they should depress the bond market, do you have enough other assets so that you can be certain of holding your bonds to maturity and not suffer large discounts?

8. Do you have a large enough sum to invest to meet requirements?

9. Have you considered the commission charge on small "lots"?

10. Are you willing to accept the responsibility for this investment and obtain the knowledge needed?

11. Would you feel more comfortable with your savings in a bank or other savings institution?

12. Have you computed the "difference" you would achieve by placing your investment in a savings institution vs. the bond market on a (1) best situation scenario (2) stay the same (inflation & interest) and (3) worst scenario?

13. Have you considered a professionally managed bond fund?
(consult with your banker or broker)

Recommended Reading
Chapter Eleven

Bonds, by Robert Lawrence Holt
The Handbook of the Bond & Money Markets, by David Darst
The Complete Bond Book, by David Darst
Municipal Bonds, by Lamb & Rappaport
How to Invest in Bonds, by Hugh Sherwood

Chapter 12

Mutual Funds

Mutual Funds have been the "darlings of the 1980s investment market. This is understandable when one realizes total assets of mutual funds tripled in the last five years! We have her a classic "chicken or the egg" type consideration. Are these funds popular because their assets tripled or

did their assets triple because there is something special about mutual funds that attracts investors?

HISTORY

Mutual funds have been around for a long time. The idea of pooling resources and hiring one professional manager can be traced to France and England over a hundred years ago. However, the mutual fund concept as we know it today was only recognized as a viable investment alternative in this country after World War II.

All mutual funds used to invest in common stock. Common stock did nothing but rise during the heady days of the 50s and 60s and so did mutual funds. They were selling at up to twenty times earnings in some instances! The recession of 1974 took the sails out of the investment market in general, but did even more damage to the mutual funds. Many mutual funds began investing in more risky and dramatic holdings and abandoned their former conservative approach. They went through a period of opprobrium until their popularity revived in the 1980s.

Stock prices in the 80s bore some relationship to book value, dividends and earnings once again. The industry initiated offerings of income and corporate and municipal bon funds to go with the original equity funds. However, the biggest seller in the early 1980s were the money market funds. These are short term holdings which at one point paid over 15%.

The concept of the "no-load" fund (no commission or fee) was developed, and cost conscious clients rushed for the bait. The bait was an unbeatable combination of convenience and lower cost. Offerings were made directly by mail to the consumer. Shares could be bought and sold (redeemed) by mail. If an investor was able to make up his mind, choosing from all the literature available to him, he could by-pass the salesman (broker) completely. Statistics showed mutual funds held their own and actually out-performed many other investments. Between 1978-1980, the pension funds (more cost conscious than ever due to high inflation rates) jumped in to the Mutual Fund Market with both feet, doubling their investment form 1.4 billion to 2.9 billion.

WHY ARE MUTUAL FUNDS SO POPULAR?

It is not surprising that the small individual investor gets poorer information and fewer breaks than the institutions or wealthy investors. To sell 50 shares with the same effort it would take to sell 50,000 is not efficient. Mutual Funds put a change to that. The "little guy", by pooling his resources with other "little guys", is able to attract the best investment advisors and funds manager in the industry; something not one of them would probably be able to afford on his own. It is the job of the Mutual Fund's advisor to evaluate the past by giving just the right amount of credence to the rate of return that has been earned by the fund compared to similar funds and the overall investment market. The fee for this advice is usually the largest expense a mutual fund faces. The relation this fee, plus the relatively minor expenses incurred with regular administrative office routine, bears to the funds assets, is referred to as the fund's expense ratio. Of course the lower the expense ratio the better. Usually that is all the expense (divided up among all the shareholders) there is in a no-load fund. In a load fund there is often a 8% to 9%

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fee so the return had better be superior to that of the no-loads. In the April 1983 issue of *Money Magazine*, mutual funds were ranked and the top "family" was Value *Line*; a no-load fund!

Convenience seems to be another reason mutual funds have become so popular. Withdrawals and purchases can be set up on a monthly routine worry-free basis. The fund redeems shares at the current NA (net asset value) with no hassle or discounts. Bookkeeping for tax purposes is done by the fund and sent to the individual investors. One certificate is evidence of shares in several different companies; much more convenient than shuffling the stock certificates of twenty or thirty companies and trying not to lose any!

However, diversification is probably the number one reason investors find mutual funds so inviting. You might be invested in several institutions, all diverse with a total of fifty to one hundred stocks spread among them. Remember the more kinds of stock you own the less you risk!

KINDS OF MUTUAL FUNDS

OPEN AND CLOSED-END FUNDS

The closed-end funds have a fixed number of outstanding shares that are traded on the open market. Usually the issuing company will not buy back their own shares. The price, as with everything on the stock market, fluctuates according to supply and demand. The price of a closed-end share bears no direct relationship to its net asset value (NAV) which is the fund's assets minus liabilities divided by all shareholders, the price is pushed up when the demand is high and drops when the demand eases.

Open-end funds are more numerous than closed. The number of shares is not fixed but is "open". The corporation can issue more shares as the demand arises. An investor buys from and sells directly to the company. Shares are not traded on the open market. The price is determined by the NAV, discussed above. Most of the Mutual Funds we'll be discussing are open-end. Open-end funds are currently the most popular.

STOCK FUNDS

These funds invest in both growth and income stocks. Growth stocks where the income received is incidental; riskier more aggressive growth stocks; and income stocks offering the highest yields where growth is secondary are typical of a diversified stock fund portfolio.

BOND FUNDS

Mutual funds invest in all or only one or two of the following types of bonds: U.S. government bonds that are risk free but offer lower yields because of the increased security; top rated corporate bonds offering a high yield but with limited risk; and finally the lower quality corporate bonds with a higher yield and more risk.

BALANCED FUNDS

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These funds try to achieve a balance in their portfolios between stocks and bonds. The traditional balance has been two-thirds stocks and one-third bonds. The income-oriented balance funds attempt to accumulate more bonds when interest rates are higher than dividend returns and vice versa.

MUNICIPAL BOND FUNDS

These funds are popular because their income is tax exempt. Investments here are classified according to the length of time the funds are committed. They can be bought as tax-free money markets (very short term); intermediate or longer term and in the category of high yield, lower grade but long term bonds.

TAX-MANAGED FUNDS

Tax-managed funds refers to mutual funds emphasizing utilities. The objective is to minimize taxes by reinvesting income instead of paying taxable dividends. That way, the investors qualify for long-term capital gains treatment.

SPECIALIZED FUNDS

An investor can purchase mutual funds that specialize in one particular market such as gold and everything to do with that one precious metal. Other funds specialize in chemical or energy companies exclusively or the stocks of other nations traded on foreign exchanges. High technology stocks have been a popular specialty. If you feel strongly about a certain industry, chances are you'll find a mutual fund specializing in it. The point to remember is that diversity is the name of the investment game and the more specialized mutual funds would no doubt add; "the greater your reward!")

DUAL-PURPOSE FUNDS

These funds offer two kinds of shares: income and capital. The income shareholder has no need for or interest in capital appreciation and so the capital shareholder gets a double benefit. Similarly the capital shareholder is not interested in current income and is happy to see it go to the income shareholder in trade. These are actually closed-end investment companies. The fund is organized for a definite period of time after which the income shares are retired at a fixed price. All the capital growth would go to the capital shareholder only at that time, the income shareholder having received all the income exclusively over the years. It is a case of "double the pleasure" for both types of investor.

LETTER STOCK AND HEDGE FUNDS

Letter stock funds consist of holding of stock from companies that are so new or small that they are not registered with the SEC (Securities and Exchange Commission). Buyers of this stock must sign a "letter" which states that they will keep the stock for a specified time before reselling.

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Hedge funds involve a lot of "wheeling and dealing" and are mentioned together with Letter Stock Funds because neither are prudent investment for the novice. They are both highly speculative mutual funds and are brought to your attention as a warning.

VENTURE CAPITAL FUNDS

Venture Capital Funds could really be grouped with the two funds mentioned above. The small non-professional investor should be warned about these funds also. They are not registered with the SEC in some instances and those that are often provide the start-up capital to other companies too new to have been tested. The estimation of the new company's ability to stand in the marketplace is left wholly to the discretionary judgment of the Venture Capital Fund's manager. To risk your investment dollars solely on one man's judgment takes a lot of courage or stupidity!

FAMILY OF FUNDS

The idea that one investment company can offer a variety of funds with different objectives has caught on rapidly in recent years. A "Family of Funds" may refer to separate corporations or a trust or may be a single corporation with a series of separate and distinct portfolios, called, not surprisingly a "series fund." This makes "switching" from one fund to another within the family very convenient. For instance you may invest in the Family's stock fund during your early years and wish to switch to an income fund upon retirement. This exchange privilege would allow a person to switch form a growth fund to a money market in order to protect his funds if he anticipates a market decline or vice versa.

YOUR GOALS COMPARED TO THE OBJECTIVES OF THE MUTUAL FUND

In analyzing your own situation you should decide the amount of risk you are willing and able to take and see if there is a mutual fund with compatible objectives and policies. The worksheet at the end of the chapter is designed to help you do just that. I would caution you in examining a fund's past performance, do so "with a grain of salt." There is no guarantee that the past will be repeated (despite Santayana) and indeed there may often be more evidence to show why it should no be. It could be that this stock has "had its day in the sun" and now it is anther's turn. There are , however, some guidelines to help you understand a fund's goals. Money market funds strive for current income without risk to principal. Bond funds emphasized stable income, whereas growth equity funds are best for obtaining capital appreciation. A retired person may prefer a combination: stock fund for inflation hedging; bond fund for durable income and a money market for capital preservation.

WHEN SHOULD YOU INVEST?

In general it is never a good idea to invest a very large lump sum all at one time. it might be advisable to put all the money in a money market fund at the beginning though, and exchange within the same family over a period of several months. As we discovered earlier, dollar cost averaging reduces risk. We referred to it as time diversification.

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People have tried to jump into stocks when the market is low and reverse at the high point. It sounds so easy to invest in aggressive funds during runaway markets and switch back to conservative holding in trading market. Unfortunately statistics have shown that market-timing just doesn't work overall. The same illusive skill (luck!) is required to pick the "hot" crap table and "cold" blackjack dealer in Las Vegas.

SAFEGUARDS

Mutual Funds are regulated by the SEC and the other investments we have discussed so far in this section. Federal law mandates that only 5% of a mutual fund's assets may be invested in securities of any single entity. They may own no more than 10% of any class of securities issued by an individual company. Mutual funds are restricted to the amount they may borrow and must distribute 90% of their net income to shareholders annually.

SUMMARY

Mutual funds are a proven and popular investment vehicle. Many people with similar objectives, by pooling their resources are able to participate in a variety of investments. Such diversification, as you well know by now, always reduced your risk. These investors can also afford better quality (higher priced) management and advice than they could hope to obtain individually. Mutual funds outperform other types of traditional investments due to their well developed objectives and the size of their pooled assets which allows them to attract top managers. Mutual funds provide convenience and diversification. Not only that, the investor receives professional management and custodial administrative and bookkeeping services, all at an unbelievable low cost. They are often the ideal investment for a person who doesn't want to take time from his profession or business to handle investments.

Worksheet - Chapter 12

CHOOSING A MUTUAL FUND

1. What do you want this fund to accomplish?
forced savings? _____
college tuition for the kids? _____
retirement fund? _____
current income? _____
other? _____

2. What size is this fund? _____
(remember large size might be good for stability but a smaller fund will achieve large capital gains)

3. How diversified are its holdings? _____
(Often diversification = less risk but less diversification can more easily result in spectacular performance up and down!)

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4. What are the objectives and investment policies of this mutual fund?

5. Analyze this Mutual Fund's Assets
a) Number of different companies
b) Size of companies
c) Primary fields of investment
d) Emphasis on investments in each of these fields
e) Balance between seasoned and unseasoned holdings
f) Proportion of bonds, preferred stock and cash

6. Are you prepared to invest regularly and long term? Mutual Funds are not the proper vehicle for short term speculation.

7. What do you know about the management of this Mutual Fund?

8. If you compare Fund A with Fund B do you know the period of time these investment records cover? What was the market environment? Was one Fund able to benefit because of spectacular growth-issues in a run-away bull market?

9. Have you checked the long term record before investing in this particular Mutual Fund? 10 years minimum.

10. Can this Mutual Fund hold its own in a bear (down turn) market?

11. Is this the best place for your investment dollars?

Recommended Reading
Chapter 12

Dow-Jones Irwin Guide to Mutual Funds, by Rugg & Hale
Gaining on the Market, by Charles J. Rolo
Money, by Michael Hayes
The Money Game, by Adam Smith
Competing for Stock Market Profits, by Paul F. Jessup

To quickly get investment information about a particular company you can often obtain toll free numbers by calling information and stating the name of the company.

Chapter 13

Real Estate

It has been estimated that 90% of all millionaires in the United States made their fortunes thorough real estate. Many financial planners look somewhat more unfavorably at real estate as an investment than I do. Financial Planning is a comparatively new profession; actually an

offshoot of the insurance industry. Many financial planners have connections either to insurance or stock brokerage houses and are naturally more familiar with those investments. Let me confess my own bias. I have been involved with some aspect of real estate for over twenty years. Real estate, unlike stocks and bonds where you are at the mercy of the market or another's management, allows you to retain a degree of control over your investment. Success may be hastened by your own creativity and hard work with the potential for profits being almost unlimited.

>THE NEGATIVES OF REAL ESTATE INVESTMENT

ILLIQUIDITY

Those who would warn you against real estate investments would to so on the basis that they are illiquid. It takes time to convert real property into cash. However, the recent advent of institutional investors into the real estate market has meant an increased liquidity because they have been able to establish certain guidelines which leads to faster analysis within the real estate community. Here I am speaking of investments in commercial real estate; shopping centers, office buildings, industrial property and the like. Income and single family residential property cannot usually be sold quickly because the investor depends heavily on subjective things that cannot be analyzed by a computer.

CYCLICAL

The health of the real estate market is tied more closely to the general health of the economy as a whole than some other investments. This is specially true in a commercial and developmental real estate. The areas of real estate with the most potential for profit, as you would expect, have the greatest risk. People always need residential real estate -- it is a necessity. However, high interest rates were responsible for the depressed housing market in the past few years (19080-83) and high interest rates are part of the cyclical problem.

VACANCY

An unexpected migration by a segment of the population from one part of the country to another can have drastic effects on the real estate market. This is beyond an investor's control buy really no more so than when he invests in aerospace stocks and bonds and government policies change. A vacancy factor is figured in on the liability side when analyzing a real estate investment. It is only when this is exceeded because of overall economic trends that a real problem can arise.

GOVERNMENTAL AND POLITICAL MEDDLING

Zoning changes, rent control, energy and new code requirement, moving a highway or construction of a new road, school or park all affect real property for better or worse.

OBSOLESCENCE

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Buildings become outdated and unable to compete with their newer counterparts which naturally reduces their value. This is taken into consideration, however, and is why a depreciation allowance is permitted.

POSITIVE ASPECTS OF REAL ESTATE INVESTMENTS

APPRECIATION

Real estate values have gone up constantly since the end of the Great Depression. The influx of foreign money into the United States real estate market attests to the general feeling that a well considered real estate investment is extremely safe because of the political stability of America. Besides providing a hedge against inflation, an investment in real property enabled the investor to pay debt with inflated dollars. The dollars he borrowed to buy his property were worth much more when he borrowed them than are the ones with which repayment is made to the lender. It is wise to remember: "Borrow during times of inflation; never lend, for you'll be short changed!"

CASH FLOW

Often real property can provide a monthly income rather like the dividends paid by stocks or interest received from bonds. Usually in order to obtain a cash flow, a considerable down payment must be made when purchasing the property, otherwise, the mortgage payments together with other expenses connected with the property, would use up all such proceeds. Alternately, cash flow may occur after the property has been owned a few years and a second or third mortgage has been paid off thus reducing the overall payments required to "hold" the property, or when the rental market has increased and more dollars are coming in monthly.

TAX BENEFITS

Although an investment should never be made solely for its attractive tax-shelter feature, those features should not be overlooked when it comes to real estate investment. I will only mention these benefits here as they will be discussed in Section Five. There are possible capital gains treatment, depreciation, interest and maintenance deductions, investment credits plus the fact that the "at risk" rule (the rule that no more may be deducted from taxes than what the investor actually has "at risk") does not apply to real estate.

LEVERAGE

Leverage is quite simply the use of borrowed funds. In real estate it has not been uncommon to use 75% to 80% of another person's money to purchase a property (usually in the form of a mortgage) more uncommon, but not impossible, is the opportunity to make a real estate investment with "*Nothing Do*wn" (title of a recommended book by Robert Allen) as described in some of the reading material recommended at the end of the chapter.

KINDS OF REAL ESTATE INVESTMENTS

SINGLE FAMILY RESIDENCE

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During the 1970s single family homes appreciated at a rate of 15% annually across the nation. That rate was even higher in sections of California and other sun-belt states. Such rapid inflation could not be expected to continue indefinitely. Because the cost of financing got out of hand, putting home ownership beyond the reach of many people, in the 1980s you should see less turnover of the higher prices residences and a pick-up in the sales of more affordable vacation homes. Young people can rent near their workplaces and reap some of the benefits of home ownership in a resort area. This would not have made sense 15 or 20 years ago but life styles today center around sports and recreation and more and more people are delaying marriage and/or children or eliminating that option altogether.

Parents have often helped their children buy their first home but it is more prevalent a practice today than ever before and naturally some new methods have originated. "Necessity is the mother of invention."

A child might borrow part of the down payment from parents in exchange for a personal note with principal and interest all due in seven to ten years. That way the parents will not have to pay taxes on the interest until they receive the money to do so. The child will be able to deduct the interest paid to the parents when he is in a higher bracket. If the parents don't charge interest or the interest charged is lower than the market dictated the IRS is likely to consider the difference between zero or low and market interest as a taxable gift. With the large allowance for gifts, $10,000 non-taxable per person could mean $40,000 would be excluded if a mother and father combined their allowances and made gifts to a child and his spouse. In all likelihood, there would be no taxable gift to pay anyway.

Another way to lend a helping hand is for the parents to buy the house and rent it to the child with an option to buy it in a later date. The rent would cover the mortgage payments, insurance, taxes, etc., and the parents would take the depreciation and interest deductions as long as the house was in their names. The rent would be taxable income but out-of-pocket expense for upkeep and maintenance could be off-set against it. Similar to this plan is the idea whereby a parent deposits enough money with a lender to make up the difference between the 10% his child might be able to afford and the 14% market rate charged by the institution. This scheme would allow the kids to qualify for a mortgage that would otherwise be unattainable. The real estate industry refers to such a solution to the high priced housing dilemma as a "buy-down" mortgage. Equity sharing is another idea which is spreading in popularity. Parents receive an interest in the house for their part of the down payment. They take title as co-owners with expenses, including mortgage payments pro-rated. The child then pays rent to the parent for the use of the parents' share of the house. Of course, the child saves more on the reduced mortgage payments and expenses than they pay in rent plus the parents get tax-shelter and a share of appreciation, which will be taxed at capital gains rates when the house is eventually sold.

Of course, the most obvious and simplest way to help is to give a gift of the entire down payment which, as mentioned above, can be done tax-free up to $40,000 in one year couple to couple. Of course, not many of us can afford to be that generous much as we'd like to be able to take the simple way out.

THE SINGLE FAMILY FIXER-UPPERS

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There is little I can add to what has been said first in books written by William Nickerson. Albert Lowry and Robert Allen and which are listed with other recommended reading at the end of this chapter. These books are easy and fun to read and I recommend them highly.

Recycling, renovating or fixing up; whatever you want to call it, the system works! This is probably the surest, safest way to invest in real estate. Perhaps because it demands more brawn than brain; more elbow grease than conjecture. You have to be able to swallow your pride and become familiar with dumps, dirty garbage cans, cracked paint and old plumbing. The less capital you have to start the more willing you have to be to do what needs doing yourself. There are hundreds of excellent " How to" books available and contrary to popular belief, city inspectors can be very instructive and even helpful when it comes to saving money.

Part of "the system" is the time-worn admonition, "buy cheap; sell dear." But buying "cheap" isn't the whole story; you must buy right! Ideally, you should purchase property in the worst condition in the best neighborhood. Location is everything in real estate. You want the worst house on the block so the surrounding property will compliment and benefit any work you do to improve your own property not vice versa.

Probably the most common mistake made by beginners is over improvement. You must know what houses are selling for in the are in which you intend to invest. You can find this out by contacting your local Realty Board, Tittle Companies or City Hall. Stop improving when the house has been brought to neighborhood standards. It is ridiculous to add a swimming pool and a tennis court to a house in an area where homes sell from $100,000 to $150,000. You will not even get back your costs.

The other trick in renovating rundown properties is to put as little of your won money into the project as possible. Use lenders' money; usually a bank or savings institution, but it could be a private party. Since 1978 there has been a good deal of talk from the real estate industry about the "new creative financing.: True, creative financing has become more pervasive during the last years as home prices soared, abut it is not a new concept, it has always been the mainstay of the shoestring renovator. There's nothing new about getting a seller to carry back a mortgage on his rundown property. The worst that could happen from his point of view is that you (the buyer) will put some time and effort into his neglected property and then default on the loan. If you can't pay as you promised whey the poor old seller just gets the renovated, or partially renovated property back, You bet he's willing! If you approach him in the right spirit he may be willing to sell you the property with nothing down. There's no mystery to it, it's just common sense.

RESIDENTIAL INCOME PROPERTY

What I said about using the other guy's money and doing work yourself holds true for residential income property too if you are short of cash. A little more "brain" must be added to the "brawn" in this area, however. You must figure out the gross income of the property you propose to buy and apply the proper "multiplier" for your area to determine the price you are willing to pay. Gross income is all the money the property brings in on an annual basis. For instance, it the property is small, three to four units, it might gross $20,000 a year. If the "multiplier" for your area in the current market is "9" you might want to pay $180,000 for the property. You would

then figure how much it would cost to improve the property so your gross income could be raised. Everyone seems to have their own rule of thumb in this area. To pick one; let's say for every $10 of improvement you should get $30 more rent or $100 more selling price. You can begin to see that if you do such and such you will realize such and such return. We're talking about the same concept we've been using with stocks, bonds and mutual funds; the actual return on dollars invested. In real estate the rate of return is the net income on dollars invested. In real estate the rate of return is the net income from the property before interest and depreciation, divided by the purchase price. For example; $20,000 divided by $180,000 = 11% rate of return.

If the property needs work but the income is already too high or even at market, pass that property by. You need to be able to add to or improve in such a way that the income will increase as a result of your work.

The next thing to consider is the net income (gross income minus expenses). Will the property carry itself or will you have to dig into your own pocket every month to meet the mortgage(s), taxes, utilities, insurance, maintenance and repair cost? But even so, remember all such losses are tax deductible as are interest payments and a certain amount of the properties' supposed loss in value over time (depreciation allowance). Real estate is valued for its tax shelter possibilities any you just may find the benefits outweigh the negative aspects. Where else can you get such a combination of capital growth and tax shelter in one package? Not only have real estate prices gone up in past years, keeping pace with inflation, but an investor's equity in the property increases with each mortgage payment indirectly paid by tenants. All this is in addition to the regular pull of supply and demand at work in a free marketplace which has kept the prices of real estate on a one way (UP) direction since the second world war. Additionally, income property requires you to have the hours of an obstetrician (plumbing and heating emergencies always seem to occur in the middle of the night) and the stamina of the head of the complaint department at you local shopping center.

DEVELOPMENT

We have seen that residential real estate can be a good investment even for amateurs who are willing to ask questions and work hard. Success or failure can be in your hands if you choose to keep control. Not so in development. You are at the mercy of contractors, architects, raw material suppliers, attorneys, lenders and even the overall political and economic situation. Development is not for the uninitiated!

COMMERCIAL REAL ESTATE

When we speak of commercial real estate and industrial real estate we refer to shopping centers, office buildings and warehouses. Just as the value of residential income property is determined by multiplying gross annual rental income by a fluctuating (fluctuating according to locality and market conditions) "multiplier," commercial real estate is valued by applying a similar market derived figure known as the "cap rate" (capitalization rate) to revenue using one of two possible methods, the pre-debt or cash-on-cash approach. Figuring what it would cost to build a new structure similar to the one you are contemplating as an investment is an alternate means of

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determining value for all types of real estate. The ideal balance is where the capitalized value of the investment approximates the reproduction cost of the property.

The key to success in commercial real estate lies in finding a property in a good location, a tenant with strong credit and negotiating a good lease. Investors not interested in managing their properties often look for triple-net leases. Under a triple-net lease the tenant, in addition to making the rental payments, is responsible for all operating expenses, debt service on the landlord's mortgage and the property taxes.

Because commercial real estate is based heavily on judgments and negotiating skill which can not be acquired overnight, this is not a suitable investment for the novice unless he is fortunate to have at his side an extremely competent broker in whom he has complete trust.

R.E.I.T.s -- REAL ESTATE INVESTMENT TRUSTS

A real estate investment trust may be either a trust or a corporation. The trustee or directors invest the assets only in real estate holdings. Each individual investor owns shares of the portfolio.

There are basically three types of R.E.I.T.s : those that own real property, those who lend money for real estate development and a combination of the two. Since shares are traded on the stock market, R.E.I.T owners find themselves with a liquid asset. This is the only form of real estate ownership that can be priced daily without an appraiser; the supply and demand of the stock market fulfills that role. Potential investors should investigate this form of real estate ownership as they would any cyclical stock (see chapter 11) with the additional warning that in general R.E.I.T. s are not widely held so the small investor may find himself at the mercy of larger stockholders whose movement could drastically affect the price of the stock.

LIMITED PARTNERSHIPS
SOMETIMES REFERRED TO AS SYNDICATIONS

A limited partnership is made up of one or more general partners who actually manage the affairs of the partnership and assume personal liability, and one or more limited partners who are passive investors with their liability limited to the size of their investment. The passive investor finds himself dependent upon the management and expertise of the general partner. Therefore, it is imperative to find out everything you can about the general partner before committing your investment dollars. Because partnership equities are not sold on a liquid market (like the R.E.I.T.s) it is wise to see that a buy-out arrangement is included in the purchase agreement, tied somehow to the fluctuating market price of something agreed upon by all at the inception. If there is no such provision, you may find you are forced to suffer a sizable loss should you need to sell your investment in an emergency situation.

Limited partnerships provide a way for the investor who has little knowledge of real estate and no desire to learn, an opportunity to participate in the benefits of appreciation and depreciation (tax deduction) with a relatively small capital outlay and limited risk. Limited partnerships are very attractive vehicles or real estate investment if you do not mind putting your investment

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beyond your own control. So much depends on the qualifications and integrity of the general partner. I, therefore, cannot emphasis strongly enough that you should proceed with extreme caution before going ahead with this type of investment, both because of the liquidity problem and the required dependence upon the general partner.

SUMMARY

On the plus side real estate provides an opportunity to leverage, attain capital growth, is a hedge against inflation and has various tax advantages. On top of this it may provide shelter (single or income residential) as well as pride of ownership.

On the negative side, it is relatively illiquid, cyclical and more vulnerable to changes in the economy than some other investments.

It is hard to "go wrong" with residential real estate if you buy the worst house or 4-plex on the block at a very low price but in a good location. R.E.I.T.s and limited partnerships can be very lucrative investments for the passive investor who has a degree of sophistication in this area and has done his homework. Real estate development and commercial industrial investments, however, should be left to the real estate professionals.

Worksheet - Chapter 13

WHAT KIND OF REAL ESTATE INVESTMENT IS RIGHT FOR ME?

Circle a number. 1 means you agree strongly, down to 5, signifying strong disagreement.

1. I would like to work with tenants. 1 2 3 4 5

2. I can do "fix up" myself. 1 2 3 4 5

3. I can and want to make time to manage property. 1 2 3 4 5

4. I like responsibility. 1 2 3 4 5

5. I have other liquid assets. 1 2 3 4 5

6. I want profits or capital gain more than safety. 1 2 3 4 5

7. I don't like passive investments. 1 2 3 4 5

8. I don't mind borrowing money. 1 2 3 4 5

9. I like to set goals and follow plans. 1 2 3 4 5

10. I like to be in control of a situation. 1 2 3 4 5

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11. I have adequate emergency funds set aside. 1 2 3 4 5

12. I have trouble putting my trust in another's judgment. 1 2 3 4 5

SCORING

If you scored 12-25 give residential income property a try!

If you scored 40 or above REITs or Partnerships may be for you.

In the 26-39 range analyze your answers carefully:

If you circled #1 or #2 for questions 4,7, 10 and 12, stay away from REITs and Limited Partnerships.

If you marked #4 or #5 on questions 4, 7,10,12 stay away from income property involving management responsibilities.

Recommended Reading
Chapter Thirteen

William Nickerson
Albert Lowry
Robert Allen
Complete Guide to Real Estate Financing, by Jack Cummings
You Can Profit form Real Estate Appreciation, by Maury Seldin
How to Borrow you Way to Real Estate Riches, by Tyler Hicks
Inspecting a House, by Alan Carson & Robert Dunlop
Real Estate Investment, by John E. Wiedemer
Tax Planning for Real Estate Investors, by Kau & Sirmans
The Real Estate Investing Profit Guide, by Michael Glasscock
How to Use Leverage to Make Money in Local Real Estate, by George Block
The Complete Real Estate Investment Handbook, by Sirmans & Jaffee
The Real Estate Book, by Robert Nessen
Prentice Hall Master Guide to Real Estate Investing, edited by Oliver Ray Price
How We Made A Million Dollars Recycling Great Old Homes, by Sam & Mary Weir
House Recycling, by Mary Weir
Professional Real Estate Investing: How to Evaluate Complex Investment Alternatives, by Fred E. Case
Rental Homes: The Tax Shelter That Works and Grows for You, by Vincent Zucchero

Chapter 14

Utilitarian Investments

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The Possibilities for investment are truly unlimited. Someone, somewhere will take any dollars you can spare for something! The vast variety of goals that people hope to attain by isolating investment dollars from spendable income is as limitless as the choice of investments. One thing all investors seem to have in common, however, is concern for the future.

UTILITARIAN INVESTMENTS

Investments in this category have certain things in common. None generate income but all would be considered a hedge against inflation. Most are status symbols capable of being appreciated for their intrinsic beauty aside from any monetary or image building value they may possess. There is risk in this type of investment. Not only could there not be a profit on resale but perhaps worth in terms of dollars may decline during the time the investment is held. There are numerous reasons for assuming such a possibility, many unique to the particular investment (such as dry rot attacking an oriental rug, etc.) but there are two reasons they all share. First is the possibility that you as an investor did not "buy right" in the first place. That is why it is so important not only to buy from a reputable dealer but in many instances it would be prudent to enlist the services of a highly qualified professional adviser and perhaps have him make purchases for you. The second reason for an investment loss may be that the property was not held long enough. Appreciation occasionally happens overnight, but normally time is required. Often commissions are involved and the costs of buying and selling may eat up profits within a short time period and indeed these overhead costs may be responsible for the losses.

INVESTING IN COINS

It is important to buy with a long-term commitment in mind. It may be prudent to start with a "type set" at fist (collection of one of each coin of a given series) but diversify as soon as possible to offset the effect of cycles in the volatile coin market. Try buying different metals; copper, nickel, gold and silver as well as coins from different time periods and locations. Always buy the best you can afford, choosing one quality coin over five of lesser quality. The worth of a particular coin is determined by its condition and rarity and has little to do with its face value or age. People sometimes purchase numismatic coins after hearing of spectacular profits as well as being attracted by their reputation as an inflation hedge. As with all investments I've labeled "utilitarian," it is imperative that you work with a well established reputable dealer. Collecting rare coins is an excellent example of combining hobby and investment.

STAMPS

Stamps, like the coins discussed above, are easy to store and transport. Most American investors are not as impressed by this fact as investors living in less stable environments might be. Gold, diamonds, coins and stamps have historically been a wise investment for those who anticipate having to flee from oppression or worse. Stamps are valued for their rarity and condition and are one of the few items in this world that increases in value due to someone's error. A printing mistake is, of course, rare and the resulting stamps are prized by collectors. Don't buy cheap packets advertised in magazines but specialize in a particular location, time period or type of stamp, such as all airmail or sports oriented or animals, etc. If you are a serious investor and care more about the possible appreciation than the enjoyment of collecting, it may be worth your

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while to hire a knowledgeable adviser or agent to make acquisitions for you, paying him a five to ten percent commission on each purchase.

DIAMONDS

What has been said about stamps and coins as portable inflation hedges which should be purchased under careful supervision, the best quality you can afford and from reputable dealers is equally true for diamonds. The problem to overcome when investing in diamonds is the 30% to 100% markup between wholesale and retail costs. The average lay investor must buy retail and sell wholesale. The other problem is, of course, the volatility of the diamond market in spite of the De Beers Organization's heavy control. The appreciation of the diamonds, even if held for a long period, must be great to overcome this handicap. Serious investors should really purchase diamonds of four carats and up. This calls for a large commitment of investment dollars and may suit the relatively affluent investor who already has other diversified holdings. The value of a diamond is determined by how well it measures up to the "4Cs": carat (weight), color, cut and clarity. The utilitarian advantage of choosing diamonds as an investment are well known. The stones can be worn with satisfaction and pride by both men and women and this is in itself a very enticing attribute of this investment. A word of caution, however; the cost of elaborate settings has been known to diminish the appreciation a particular gem may have achieved over time.

PAINTINGS, PRINTS AND PHOTOGRAPHY

Young people and corporations have entered this field in remarkable numbers over the past ten years looking for an inflation hedge and appreciation of their assets. Of course, a side benefit is the beautification of the surroundings, whether corporate headquarters or home, while the investment is given time to increase in value. Naturally, there is risk, especially if works of a relatively new artist are purchased. Works of a deceased artist (signifying a limited supply) who has an already established reputation in the art world, is probably a more secure investment, but, depending on the artist and the work, will probably cost more. In many cases, especially when contemplating large capital outlays, it is wise to engage the services of an adviser. Many would suggest that you specialize in one area or built a collection around one theme but buy the works of a variety of artists. It is well to remember that a good drawing or print by the same artist may be worth more than a poor painting.

Photography has gained in popularity because of its relatively low cost although retaining the same potential for appreciation and immeasurable pleasure ownership of paintings and prints offers.

ORIENTAL RUGS

Oriental rugs or carpets, are hand-woven products of the Near, Middle and Far East, the Balkans and the area between the Black and Caspian Seas. Their value is based on age (over 100 years is considered an antique and can enter the U.S. duty free), quality of construction (refers to density and fineness of weave), size (the larger the better), and place of origin. The celebrated Persian rugs are products of Iran and most sought after by some collectors while other prefer the Chinese rugs which are more readily available nowadays (1983). To maintain the value of oriental rugs

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they should be turned once a year and professionally cleaned every five years. Stay away form "traveling" auctions, although estate auctions run by a reputable auctioneer established in your area may yield some good values. Department stores are recommended places to buy, only make certain you are getting the "real thing" for investment purposes, not machine made copies. As with all "utilitarian investments," it is wise to have your rugs revalued for insurance purposes on a regular basis and keep pictures of them in a safe place.

ANTIQUE FURNITURE

Collecting antique furniture is a great way to fill the need for household furnishings, investment and hobby at one fell swoop. Remember to be classified as an antique the article must be 100 years old at least. The value of an antique depends first of all on its verifiable authenticity. Secondly, the quality and construction of your particular piece, followed by consideration of age and locality. Although it is a good idea to make acquisitions at auctions rather than pay the retail markup, it may be even cheaper to engage someone knowledgeable to handle such purchase for you. One word of caution from a mother of five; because of maintenance and preservation of your investment this is obviously a poor investment for people with young children.

GOLD, SILVER, PLATINUM

It is a borderline decision to call these metal "utilitarian investments," although it is true they are used for jewelry, eating and serving utensils and in industry. There is a worldwide market for gold and silver making them more liquid than most investments in this category. However, platinum is traded only on one U.S. commodity exchange. There are several forms an investment in one of these metals might take. The most conservative being the purchase and physical holding of the metal itself. Many people

have in their possession gold Krugerands (South Africa), or Maple Leafs (Canada) and bags of junk silver (American pre-1964 coins). It is not wise to buy commemorative sets privately minted or actively promoted "wafers" because of the high premium charged over the bullion price. Investors concerned with preserving capital and purchasing power should lose nothing by holding the metal long-term and using the dollar-cost-averaging concept discussed elsewhere. These metals are notorious inflation hedges and although there is potential for loss in the short run, history shows they have appreciated over the long haul. Many advisers recommend a certain portion of every client's portfolio include these metals-- especially gold-- to balance stocks and other investments that may sour in response to bad national or worldwide economic news or disaster. Because bad news pushes gold up it is often uses as an insurance or defensive investment.

A less conservative investment in gold, silver or platinum is to purchase mining shares. The facts that these stocks pay dividends is an attraction for some people. An even more speculative investment in these metals would be the purchase of highly leveraged future contracts. There are many excellent books written about investing in precious metals. (See recommended reading list at the end of this chapter.)

BONUS-- A FANTASY-- INVESTING

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IN MOVIES AND THEATRICAL PRODUCTIONS

I realize that you, the average person reading this book, is never going to invest in motion pictures or theatrical productions because the minimum amount required starts at a low of somewhere around $25,000 ranging up to more than $200,000 a unit (piece of the action), but wouldn't you like to dream about it?

The main attraction is the opportunity to participate is a fantasy. There is glamour surrounding the motion picture industry and even if you never get to actually rub elbows with the stars, directors and producers whose names you see on the screen, a certain amount of excitement does rub off. Perhaps the fantasy is that in return for your $50,000 or $100,000 you're going to make millions. Ridiculous but not impossible. If you only could have invested in Gandhi, Tootsie, E.T. or Star Wars!! This is perhaps the investment with unlimited possibilities, for certainly there is little relationship between the size of the investment and the potential profits. Sure a stock can skyrocket and an oil well can turn out to be a real gusher but the possible profits from such good fortune can be more easily predicted and calculated than can profits form a block-buster movie. Records are constantly being broken in this area and there are T.V. and videotapes and other subsidiary profits. Remember, it is customary for the investor to share in 50% of the profits and this can be accomplished by limiting risk by investing through a limited partnership. Don't despair, even if you don't know any producers personally you can gain access to these investments through the major investment houses. You should be aware that the brokers' commission generally runs 8% to 10% of your investment, but you are paying for advice and guidance in an area in which you are very likely a novice.

Although unlimited profits coupled with limited risk may sound good, the odds are so weighted against success in this industry that many investors in the past went into this type of investment hoping to deduct losses larger than their individual investment. This practice has been stopped by Section 465 of the Internal Revenue Code known affectionately as the "At Risk" rule which basically says that a person cannot declare losses beyond the amount of his investment in the project.. Profits, should there be any, are treated as ordinary income rather than enjoying the benefits of the lower tax rates accorded capital gains. There are, however, investment tax credits and depreciation allowances but it should be readily apparent that possible tax advantages are not a motivating feature of this investment.

If I had a spare $25,000 bill laying around and I only had a couple of years to

live , I might prefer the aura of investing in a motion picture to that of placing a bet in Vegas. Both are long shots and both offer the possibility of making a disproportionately high return in a relatively short period of time. To other people the appeal is the intangible benefit of being associated with the production of an artistic work. This is the motivation for many benefactors. It would appear that the majority of investors in this industry must be prepared to lose and get a thrill or some sense of accomplishment wholly divorced from economics.

Perhaps you have your own scenario for making this kind of investment. If all criteria should come together-- well, bon chance!

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SUMMARY

If you are a novice investor rely on a knowledgeable adviser until you have reached a certain investment goal. If you're full of curiosity and have a spirit of adventure, go ahead and indulge it by testing some of the more exotic investments, like horses, oil/gas, options, futures, commodities, etc., but only with "risk" or "mad" money. You never want to throw money away (except as a benefactor when you know the project is not economically sound but it is undertaken as a cause- a contribution to society as discussed briefly in the discussion of motion picture investing), so when you have graduated from total dependence on your advisers' recommendations and want to experiment on you own take Syde P. Taccfl with you. In fact, use Sydl to see that your adviser is doing his homework; never become totally dependent on anyone! Before you commit your dollars to any investment see how it measures up in terms of *S*ecurity; *Y*ield; *D*iversification; *L*iquidity; can it provide *P*rotection form creditors by making it in a trust, for instance; Period of time it should be held; *T*ax advantages, if any; use as an Inflation hedge, Callability; Convenience; can it be used as *C*ollateral; can you afford the *A*mount needed for this investment; does if offer **F**reedom from worry and make sure it's *L*egal!

The "utilitarian investments" discussed here have been categorized to some extent in the following worksheet which you should adopt to your individual situation.

Worksheet - Chapter 14

By now you, should have a pretty good idea of what you personally are looking for in an investment. Write that down in your notebook. The investments discussed in Chapter 14 are listed here with a few characteristics of each placed in a "PLUS" or "MINUS" column. Assign your own plus and minus system to these and any other investments you are considering. For instance, if you believe inflation is under control "inflation hedge" would not go in your particular "Plus" column. If you don't need current income the fact that no income is generated by an investment would not go in your "MINUS" column, etc.

Investment	**"PLUS"**	**"MINUS"**
Coins	Inflation hedge sm. amt. needed moderately liquid portable	fluctuating market needs adviser risk no income
Stamps	hobby ibid.	ibid.
Diamonds	inflation hedge portable pride of ownership	large amt. of $$ needed high markup ibid.
Paintings	inflation hedge pride of ownership	amt. needed ? risk of appreciation need adviser no income

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Prints	ibid. cheaper than above	risk of appreciation need adviser no income
Photography	ibid.	ibid.
Rugs	inflation hedge pride of ownership	amt. needed? must be maintained no income
Antiques	ibid.	ibid. may need adviser
Precious Metals	inflation hedge liquid	no income fluctuating market possible regulations
Movies &	tax advantages glamour potential high,fast profits altruism	high risk large amt. needed no salvage value

Recommended Reading
Chapter Fourteen

Encyclopedia of Investments, by Marshall Blume & Jack Friedman
The Commodity Futures Game, by T.W. Stone
How the Experts Buy & Sell Gold Bullion, Gold Stocks & Gold Coins, by James Sinclair & Harry Schultz
Guide to Antiques & Collectibles, edited by Thomas Hudgeons III
Know Your Collectibles, Antique & Collectibles Price List, by Ralph & Terry Kovel
Options As A Strategic Investment, by Lawrence Macmillan
The Commodity Futures & Market Guide, by Kroll & Shisko
How to Buy & Sell Gems, by Benjamin Zucker
How to Invest in Strategic Metals, by Bohdan Szuprowicz
How to Trade Put & Call Options, by Lawrence Rosen
Investing in Natural Resources, by Walter Youngquist
The Fastest Game in Town; Commodities, by Mark Robert Yarrry
The New Options Market, by Max Ansbacher
Stamps for Investment, by Kenneth Lake
Your Gold & Silver, by Henry Merton
Practical Guide to Antique Collecting, by Geoffrey Wills
The Stock Options Manual, by Gary L. Gastineau
How to Buy Gold, by Timothy Green
How to Invest in Gold Stock & Avoid the Pitfalls, by Donald Hopp

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Section Four
Retirement

Chapter 15
What is Retirement?

RETIREMENT YEARS CAN AND SHOULD BE FULFILLING

Before 1937 only the wealthy could look forward to retirement. With the advent of the social security system and the proliferation of pension and profit sharing plans, retirement has become the province of the average man.

Many people dream of traveling, improving their golf score, sailing, fixing-up the boat, antique car or house they way they always envisioned, gardening, painting, working on that stamp or coin collection or maybe getting more education at the local college and branching out into an entirely new field. An old Jewish Proverb says, "For the ignorant old age is as winter, for the learned it is a harvest." There is now ample evidence to support what was at one time only speculation; that being active in body and mind prolongs life. Taking an interest in living is necessary for health and happiness. Man seems to need to feel useful. We hear so much about the dangers of stress but total lack of stress boredom-- can also menace your well-being. it only goes to show what the Ancient Greeks knew thousands of years ago, that the "golden mean"; the midpoint between extremes, is the surest way to health and happiness. Too much of a good thing, even relaxation, can be harmful. Lying in bed or sitting in the sun doing nothing most of the day is a luxury when we are on vacation because our bodies and minds need that rest, and it may even feel great for the first few weeks after you retire; no longer having to rush for that 7 a.m. commute - but something purposeful, meaningful must soon take its place or boredom and discontent will set in. I once read that one must not lose desires. They are mighty stimulants to creativity, to love, and to long life. Henry Thoreau put it this way: "None are so old as those who have outlived enthusiasm."

NEVER TOO EARLY TO PREPARE

Most of us start fantasizing in our forties about all the things we're going to do when we retire, but those ambitions will remain fantasies with no chance of attaining reality unless preparation is begun early. The "early bird" may catch the worm but let me show you an example of what the "early investment bird" can catch!

With an investment of $2,000 per year at 10%, Sue , at age twenty, begins providing for her retirement. Twenty years later, at the age of forty, she has invested $40,000 (2,000 per year for twenty years) which has grown to $126,000. Meanwhile Mary consumed all her income at age twenty but began investing using the identical procedures as Sue but waited until she was forty years old. Sue continues with the same program. Twenty years later (and another $40,000) Mary is sixty years old and has an investment worth $126,000 but Sue who is also sixty years old now has an investment worth, not double Mary's, or $252,000 as you might expect since she put in

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twice as many investment dollars over the years, but Sue has at age sixty an investment worth $973,704!! No, it's not a misprint. Sue's total investment of $80,000 worked for her over the years, feeding on itself, interest earning interest until it was worth $973,704!! More will be said about compounding interest. That was the "magic" that occurred in the example for both Mary and Sue.

RESULTS WITH COMPOUNDING

SUE			**MARY**		
age	cumulative contributions	cumulative total	age	cumulative contributions	cumulative total
20	$2,000	$2,200	--	--	--
25	10,000	13,432	--	--	--
30	20,000	35,062	--	--	--
35	30,000	69,900	--	--	--
40	40,000	126,004	40	2,000	2,200
45	50,000	216,364	45	10,000	13,432
50	60,000	361,886	50	20,000	35,062
55	70,000	596,254	55	30,000	69,900
60	80,000	973,704	60	40,000	126,004

I realize there is a great temptation to readers still in their twenties and thirties to skip this section on retirement, but really the earlier retirement planning is begun the happier those later years will be. You cannot tell if a man had lead a lucky, successful or happy life until the end has been reached.

Oscar Wilde once said, "When I was young I thought that money was the most important thing in life; now that I am old I know that it is." Of course, that was said in jest, but it is amazing how many people minimize the important role money will play in their old age. In many cases it is not being replaced, only consumed and that its why all the assets you have upon retirement should be working for you bringing in interest, dividends or rents. Even though you may be active, not may of you will also be generating income at the same level you did during those most productive pre-retirement years when you had reached the top of your field.

I recently heard of an organization in New York City which attempts to salvage the latent talents and skills of seniors. "Senior Achievers Enterprises" is dedicated to providing our older citizens

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with productive work in exchange for reasonable compensation. Hopefully organizations like this will someday replace senior citizen centers which are generally non-productive in the sense that the training and years of experience of most seniors is not utilized to the fullest in watercolor classes, bird watching, folk dancing and card playing activities.

I realize it is hard for many young people to look ahead. More and more Americans live for today with the hope that tomorrow will take care of itself. The excuse most often heard for living only for today is the threat of nuclear war. "We may not be here tomorrow," it goes, "so why plan for it?" There have been fears of the world ending which have tempted every generation into that kind of thinking. It is only recently and in America, however, that the government itself has fostered the "live for today" attitude by subsidizing consumption and penalizing savings, by offering tax deductions for consumer interest payments.

The fact is we as a nation are just beginning to recognize the fallacy of such short-term thinking. If we are to compete with nations such as Japan, whose people habitually sacrifice short-term desires for the good of the long-run, we must re-educate our politicians. Individual citizens must also adopt long-range planning when dealing with their own economic realities.

INFLATION

A few years ago the destructive force of inflation was more visible than it is today. As I write this our inflation rate is down to less than 4% so it is easy to discount inflation as a threat to our future security.

For years inflation was 3% to 4%. Interest rates, which generally run about 3% higher than inflation were 6% to 7% during those same years. The present high interest rates, in spite of low inflation, reflect the huge government deficit that must be resolved and consequently, or additionally, expectations that inflation will rise again in the not too distant future.

You probably know of many seniors on a fixed income who had savings at 5 1/4% when inflation was running at 13% to 14%. They saw the purchasing power of those dollars diminish before their eyes.

Most people realize by now that high prices and high wages are results, not causes of inflation. Inflation occurs when an increase in the money supply is unaccompanied by a corresponding increase in the production of goods and services. For example, let's take the imaginary town of Contentment, population, 1,000; full employment; no rich; no poor but the entire population is quite content. Suddenly a dozen limousine drive up loaded with wealthy tourists who like the quaint little town so much they decide to stay. The price of food, lodging, services suddenly zooms up. There just isn't enough to go around. The wealthy tourists have increased the money supply without increasing goods and services; the result is skyrocketing prices-- inflation!

In America the money supply increased more than 700% from 1945 to 1980 and the average price for goods and services increased 1200%. For example, a cup of coffee went form $.05 to $.50, magazine from $.05 to $1.25, movies from $.25 to $3.25, and an average house from $5,000 to $80,000.. Production rose, of course, but not at the same rate. Both the government and

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its individual citizens expanded their desires faster than their real incomes. Deficit spending was possible for so long because the Federal Reserve, though the banks, made money available. When the policy was reversed by the tight money policies of Paul Volcker (Head of the Federal Reserve beginning in 1980), of course, interest rates went up because enough money was no longer available to meet the demands of eager borrowers. We should all be grateful to Paul Volcker for calling a halt, that is all of us who avoided bankruptcy and unemployment!

This is an extremely simplified explanation of the halt of inflation. Actually, inflation is an interdependent worldwide phenomena and it cannot be licked permanently as long as our huge deficit budgets remain. If I hadn't lost my respect for "experts" who often disguise their own ignorance by claiming something is "too complicated to go into," I'd make that same claim right here. One thing is crystal clear; we cannot trust the politicians to discipline themselves!! Although we hope for low inflation we must all hedge against the possibility of reinflation.

UNCERTAINTY CALLS FOR SHORT-TERM INVESTMENT STRATEGIES

In a fluctuating market, diversifying your investments is more important than ever. In uncertain times like the early 1980s have shown themselves to be, the best advice may be to invest short-term and plan long-term. It is not wise to get locked into any investment over a long period of years when so many "experts" differ on the call of interest (up? or down?) and on whether inflation has really been licked.

WHAT DOES RETIREMENT MEAN TO YOU?

We began this chapter with a discussion of the fantasies people have about retirement. In the worksheet that follows you will attempt to come to terms with your own dreams about the future. Once your idea of retirement is defined steps can be taken, prudent investments made and skills and education acquired if they should be the ingredients necessary for the fulfillment of those dreams.

Some expenses connected with health care, entertainment and travel may rise upon retirement, however many more expenses will disappear. Smaller living quarters with their accompanying smaller utility bill; lower or a paid-off mortgage and life insurance policies; no more commuter and other job related expenses; lower food bills and use of dollars once siphoned off to support the now self-sufficient kids are a few benefits you might look forward to. In addition you'll find Medicare will go a long way towards lowering hospital and doctor bills. Tax breaks will also be a part of your status as a senior and should be remembered in your planning. Don't forget the "exemption" for persons over 65 and one time break on selling your residence and credit up to 15% of your retirement income, etc.

THE BEST THING TO SAVE FOR YOUR OLD AGE IS YOURSELF

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All the skills you have built up over a lifetime can be put to good use in your retirement years. In most cases, you have the time, you only need the confidence and determination. Now is the time to review chapter five.

What you're able to produce for your own use is tax-free and also reduces your expenses. What you can make or do for others can make you self-sufficient, give you a sense of pride and worth, a circle of admiring friends and customers and, of course, great pleasure.

FREE ADVICE CAN BE EXPENSIVE

Unfortunately, there are profiteers waiting to prey on the fears and anxieties of older newly retired people. Salesmen, annuity peddlers, bank employees or anyone who acts beyond the scope of his expertise will only mislead you. Never take technical advice from just anyone because it is "free". Huge profits may well be the motivation of unscrupulous persons who smilingly offer this ultimately very costly advice. An hones-to-goodness desire to help may also be the motivation, but if the person is not an expert in the area in which he offers advice good motives will not make him any less a danger to you. On the other hand, if you can tell the difference between good and bad advice then you probably don't really need it anyhow!

SUMMARY

Chance are you will live long enough to retire and you had better make preparations for that time; intellectual and emotional as well as financial preparations. The earlier you set funds aside for growth towards retirement the cheaper your retirement will be because those funds have a longer time to compound. Don't be too certain that inflation will still be under control when you retire. Diversify your retirement investments including some traditionally inflation hedged such as hard assets. Don't get into long term commitments because the present market is far too volatile, on the other hand don't " park" all your assets on the sidelines either (money market funds or savings accounts, etc.) waiting until you're shown some 'sign" as to what the stock and real estate markets are going to do and which way inflation and the national debt will turn. Diversify time as well as investment vehicles. Have some investments maturing in less than year, two or three years and some in five years. Don't go out more than five years without a possible escape. The following worksheet will help you discover what you expect and desire your retirement to be.

Worksheet - Chapter Fifteen

1. When do I want to retire?

2. What do I intend to do with my time when I retire?

3. What is my anticipated standard of living with regards to?

housing?	food?	travel?	entertaining?
clothes?	automobiles?	charity?	other?

4. What inflation rate do I anticipate between now & retirement?

		CURRENT BUDGET	BUDGET WHEN I RETIRE
Housing Costs	mtg. pymt or rent	_____	_____
	property taxes	_____	_____
	insurance (HO)	_____	_____
	utilities	_____	_____
	maintenance	_____	_____
Food	regular meals @		
	home	_____	_____
	restaurants	_____	_____
	at home entertaining	_____	_____
Transportation	car upkeep	_____	_____
	ordinary gas cost	_____	_____
	auto insurance	_____	_____
commuting expense	gas	_____	_____
	parking	_____	_____
	tolls	_____	_____
	airfares	_____	_____
	train, bus, other	_____	_____
Life & Other Insurance	Premiums		
	(except HO)	_____	_____
Investment Savings		_____	_____
Medical Expenses		_____	_____
Education, Books Papers, Magazine Subscriptions		_____	_____
Travel & Entertainment (Including Vacations)		_____	_____
Miscellaneous		_____	_____
		==========	==========

Recommended Reading
Chapter Fifteen

Strategies for the Second Half of Life, by Peter Weaver
The Best Years Book, by Hugh Downs & Richard Roll
Where Will You Live Tomorrow, by Sumichrast, Shafer & Suichrast
Tax Tactics for the Retired, by Terry & Susan Schandel
Don't Die Broke, by Melvin Jay Swartz
60 Plus in California, by William & Laurie Wishard
Public Policy and the Aging, by William W. Lammers

Chapter 16
What is Available?

The time when one could be wholly self-sufficient, if there ever was such a time, may be over. Of course, I believe and would encourage you to consider that individual savings and investment programs, if undertaken by citizens across the nation, would be the best preparation for retirement. The problem is that those who save and invest are asked to provide for those who don't. (Remember the fable of the grasshopper and the ant?) The ever-increasing burden of local, state and federal taxes reduces even the willing ant's ability to save and invest. So sad as it may appear to some of us, the truth is that the prudent , popular and in many cases the only way to provide adequately for one's retirement is to rely on (1) self, (2) employment related plans and (3) government programs (social security). (1) Was discusses in Section III of this book relating to investments in general and in Section I where sills and personal abilities were analyzed. In this chapter individual IRA and Keogh plans are introduced. (3) Has been taken care of in the supplemental reading list at the end of this chapter. Many excellent books have been written anticipating your questions concerning our social security system. The main emphasis of this chapter is on (2) "employment related programs."

PENSION PLANS

Pension plans are a way of distributing an employee's compensation over his entire lifetime, even after he has stopped working. In the past, most pension plans were "unfunded," which meant that retire employees were paid benefits out of a company's current earnings. Presently the majority of pension plans are "funded," the funds being set aside in a trust to grow and accumulate enough asset to take care of already retired workers and those getting ready to retire. Some plans provide for early retirement with reduced benefits but usually benefits are not increased if one elects late retirement and some plans even mandate retirement at a certain age.

A "qualified" plan is one which meets certain minimum standards established by ERISA (Employee Retirement Income Security Act of 1974) and by doing so offers several tax advantage to the participants. The employee defers taxes until benefits are actually received upon retirement and meanwhile they continue to multiply in a tax-sheltered environment. The employer takes a current tax deduction for his contributions as they are made.

VESTING

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In contributory plans where the employee pays a portion of the cost, if he should terminate his employment before retiring he is entitled to a refund in the amount of his contribution. What, if any, portion of his employer's contribution he is entitled to depends upon the vesting provisions of that particular plan. (Vesting means employee's right to benefits.) Some plans provide full vesting after ten years on the job and none before that time. Others allow for 25% vesting after five years, and additional 5% per year for the next five years followed by five years of 10% vesting per year. It takes fifteen years for full vesting instead of ten but at least if you terminate your employment at the end of nine years you've got something to show for it from the employer. Another option is referred to as the "rule of 45". After a minimum of five years employment the employee is awarded 50% of his pension rights when the number of years of employment plus the employee's age equals 45. Example; six years of service by a 39-year old employee would result in 50% vesting. Another way to achieve 50% vesting is by ten years of employment with no regard to age. For example, a thirty-year-old who had been with the company ten years would be 50% vested. Everyone is considered fully vested after fifteen years under the "rule of 45" option. These are the minimum acceptable vesting provisions allowed by ERISA but more liberal plans exist.

DISABILITY

Many private pensions provide for disability. Some grant benefits at an actuarially reduced rate if an employee is forced to retire early form his job because of a permanent disability. Others allow benefits to accumulate just as if the employee were still on the job and then pay full retirement benefits when the disabled employee reached normal retirement age. Another way to handle the situation is to pay so much a month for each year of service or to provide an immediate benefit as a percentage of the salary the employee was receiving at the time of his incapacity. These provisions should be checked in your own plan as there is a great deal of variation and eligibility requirements that are not standardized.

THREE BASIC TYPES

Pension plans may be divided into three main categories: (1) the defined-benefit plans which are most attractive from the employee's point of view because they commit the employer to provide determinable, specific benefits; (2) the money-purchase plans in which there are definite mandated employer contributions and the employee receives whatever benefits his pension account will purchase at the time of his retirement and (3) the target-plans which make no firm commitments or enforceable promises buy try to provide certain benefits.

Defined-benefit plans promise fixed benefits under various formulas. Under the flat-amount formula all employees meeting some minimum qualifications receive the same exact benefits. The flat-percentage formula relates benefits strictly to a percentage of earnings where the flat-amount-unit-benefit formula concerns itself with years of service. A predetermined flat amount is given for each year of employment. A variation of this, called the percentage-unit-benefit formula awards a percentage of 1% or 2& of one's former salary instead of a flat amount for each year of service.

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With the enactment of ERISA in 1974 the commitments demanded of employers were expanded to the point where a failure to live up to such a commitment could threaten the very life of a company. ERISA demanded among other things, earlier eligibility, faster vesting, , minimum funding, amortization of funding deficiencies, insurance of benefits and contingent liability of up to 30% of the entire net worth of a company if a company ever wanted to terminate a plan. Such legislation naturally discouraged defined-benefit plans by making the cost prohibitive.

An analogy comes to mind: Everyone would agree that purified water is desirable and worth paying a high price for, but at some point removing the last bit of relatively harmless impurities would be so costly that a company could not stay in business and water would be denied completely to such demanding consumers. The standards set by ERISA are also desirable but wouldn't defined-benefit plans with a few "impurities" have been better than none at all? Many employees now think so. Because of ERISA's exaggerated demands, almost 30% of all plans were terminated in the 1970s. More and more companies switched to target and money-purchase plans where the employee is at the mercy of the investment market. Decreases in trust assets are now the employee's risk not the employers' who under the defined-benefit plan had to increase their contributions if trust assets decreased in value below a certain level.

I'm reminded of something Winston Churchill once said: "Some see private enterprise as a predatory target to be shot, others as a cow to be milked, but few are those who see it as a sturdy horse pulling the wagon."

PROFIT SHARING PLANS

Business with fluctuating income often prefer to relate their retirement plans to profits rather than payroll. Profit sharing plans are believed to give the employees a personal interest in the business and to draw management and employees closer together.

The employer takes a tax deduction for all contributions made to the plan and the employee gets full 100% credit for all such contributions which compound tax free until withdrawn. Several years ago profit sharing plans were responsible for making many employees fairly well-off. It was a combination of large contributions by both employer and employee plus the appreciation of the fund's capital and the forfeiture of unvested portions of accounts of ex-employee participants. But lately no one has gotten rich from profit sharing plans. In a great majority of cases employer contributions have trickled to almost nothing, the employee has been hard pressed to make ends meet let alone put aside for his retirement and on top of that the funds have done poorly showing losses rather than gains in the unsteady market of the past five years.

A desirable feature of most contributory plans is that they offer either loan or withdrawal benefits or a combination of both. Distributions are legally permitted after two years but each plan has its own unique restrictions. Some plans only allow withdrawals of employee contributions, others restrict withdrawals to a percentage of the amount vested an then only in an emergency situation. A loan rather than a withdrawal is preferable because borrowed funds are not considered income and are therefore not currently taxed as withdrawals would be. Not only that, the employee can deduct from current income taxed the interest paid on the loan.

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STOCK PURCHASE PLANS

Under one version of this plan all employees (non-discriminatory) meeting certain qualifications are permitted to buy company stock at a discount of up to 15%.

Under the Economic Recovery Tax Act of 1981 (ERTA) incentive stock option plans can also be made available on a discriminatory basis to certain employees, usually the highly paid executives who would prefer the tax benefits such a plan offers over an increase in current compensation which would be taxed as ordinary income. These incentive plans have requirements which must be met: the option price is not a discount (as in the non-discriminatory plans) but must equal or exceed the value of the stock as of the option date; the option must be exercised within ten years and the value of the stock for which options are granted cannot exceed more than $100,000 in any one year. Taxes

are paid only when the stock is sold and usually at capital gains rates which means 60% tax-free.

SERPS

Supplemental Executive Retirement Plans (SERPS) are another form of deferred compensation which were initiated to pay additional benefits to top level executives in order to increase the level of retirement income beyond that contemplated by the basic retirement benefit plan formula.

EMPLOYEE STOCK OWNERSHIP PLANS (ESOPS)

In order to encourage use of ESOPS, ERTA provided a tax credit against payroll for companies adopting them. A corporation establishes an employee stock ownership voting trust which borrows money on the employers' guarantee and uses that money to buy company stock. The corporation makes tax-deductible contributions to the trust which in turn cover the loan payments. In this way the company ESOP can raise capital by purchasing company stock with borrowed funds. The company then pays off the loan with tax deductible dollars. Beneficial ownership of the stock passes to the employees according to a set vesting plan but actual possession remains with the trust to grow in a tax-free environment until retirement. Employees may be required to grant a first right of refusal to the company at fair market value before selling outright to a third party and the trust or employer company may be required to purchase securities that cannot be sold at a fair price based on a time and valuation formula on the open market; in reality a "put option."

The idea behind ESOPs may be best expressed by an anecdote. A wealthy capitalist employer put up with the outspoken radial politics of a certain employee because that employee did an excellent job. The employee continually attended meeting of fanatical groups and reported their activities and spouted slogans to everyone in the office following such meetings. One Thursday after attending the usual Wednesday night communist group session, the employee was strangely silent. The employer questioned him and discovered the employee would no longer be attending those meetings. "What happened?" asked the employer. "A speaker told us that if all the wealth

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in this country were equally distributed tomorrow, each person would have $5,000." "Well---?" prompted the employer. "I have $10,000 saved," blurted the employee.

A large portion of our society is deprived of power because they find themselves living off and at the mercy of other people. Louis Kelso, the originator of ESOPs, believes this in one of the most destructive forces working against the overall economic health of our nation. People who have no real stake in producing wealth beyond wages are not living up to their potential.. The ESOP theory holds that if everyone had a "piece of the action," in this case a capital investment in the company, our entire economy would benefit.

TAX-SHELTERED ANNUITIES (TSA)

TSAs are excellent programs for retirement planning but unfortunately they are available to only a few people. To participate one must be employed by public schools or tax-exempt institutions organized specifically for educational, scientific, religious or charitable purposes. The participants can purchase annuity contracts, retirement income insurance policies or mutual funds all with before-tax dollars. Up to 20& of an eligible employee's salary can be out into a TSA. When withdrawn at retirement or sooner the benefits from a TSA are taxed at ordinary income rates.

THRIFT OR SAVINGS PLANS

A derivative of the other employee benefit plans is the thrift or savings plan. The employer's contributions are based either on company profits or the employees own after-tax contributions. Often the employer's contribution escalates with length of service. (For instance, $.50 on a dollar for the first five years and then matching dollars from then on). Remember the employees not taxed on the employers' contributions so that amount together with his own contributions compound in a tax-free environment. The employee's contribution is mandated by the plan and should be set at less than six percent of compensation is required then the Internal Revenue Service considers this to be preemptively (can be refuted with facts) a showing of discrimination in favor of the highly compensated participants in the plan. The reasoning here is that the lower paid employees are having trouble just making ends meet and if contributions are set at too high an amount they will not be able to participate and the plan will benefit only the top salaried employees.

SIMPLIFIED EMPLOYEES PENSIONS - SEPs

In 1978 Congress decided pension plans needed to be simplified so they came up with an IRA format subject to special rules. Simplified pension plans allow the employer to contribute to an employee's account the Keogh limits (in 1983 15 percent of an employee's salary or $15,000). The plan contemplates simplified employer reports with significant reduction in the amount of paperwork required.

SALARY REDUCTION PLANS

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If you should happen to work for a company that has a salary reduction plan, you might just have the best of all possible worlds. There aren't many around just yet but more and more companies are thinking along this line. Like the savings plans, a portion is withheld from your salary but these dollars being invested for your benefit are pre-tax dollars!

Each company sets its own limits on how much an employee can "sock away" (2%-10%) and most companies do some form of matching. Although the name doesn't imply this, the fact is it is possible to take home more dollars after the deduction because the investments may put you in a lower tax bracket with less withholdings required from your adjusted pay check. This plan is especially good if you expect to leave the company in a few years because there is a penalty for withdrawal in such a case although you cannot withdraw sums for other reasons without a tough proof of financial hardship. You must take the money with you when you leave the company and you can use the "ten year averaging" or "roll over" within sixty days.

KEOGH OR HR-10 PLANS

Under the Keogh Act of 1962, amended by ERISA in 1974 and then again in 1981, a self-employed , unincorporated individual may set aside before taxes each year, 15% of earned income or $15,000, whichever is less. In 1984, those limits will be raised to 20% with a $30,000 maximum.

Employees putting $1,000 hours or more into the business must be covered if they have been employed three years and at least 7 1/2% must be contributed by the employer to the account of any employee making over $100,000. Vesting is immediate and all proceeds of his account can be "rolled over" to an IRA (discussed below) upon leaving the business.

The money in self-directed plans can be invested in almost anything except hard assets such as diamonds and precious metals for instance. Mutual funds are a popular choice. Many banks and brokerage houses have investment plans set up especially for Keogh accounts. You are not taxed on the capital or its earnings, which compound in a tax-free environment, until the funds are withdrawn, which cannot be before age 59 1/2 without penalty and must begin by age 70 1/2. Distributions may take the form of an annuity but lump sum distributions may avoid the alternative minimum tax by electing a special 10-year averaging option. Alternative minimum tax and 10-year averaging are discussed elsewhere.) Defined-benefit Keogh plans have been available since 1974 but because of actuarial costs and complications they are rarely used.

The following example illustrates how great an advantage it is to be able to invest with before-tax dollars:

Mr. Dim and Mr. Bright, both age 45 and in the 39% tax bracket, decide they can afford to put $6,000 a year aside for their retirement. They both anticipate a 10% earning on their investment. Mr. Bright uses a Keogh Plan and Mr. Dim does not. The chart below shows who will have the more carefree retirement.

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MR. DIM

age	contribution	taxes	earnings	worth
45	$3,660	$143	$366	$3,883
50	3,660	998	2,559	27,155
55	3,660	2,148	5,509	58,446
60	3,660	3,695	9,474	100,517
65	3,660	5,774	14,805>	157,084

MR. BRIGHT

age	contribution	taxes	earnings	worth
45	$6,000	$0	$600	$6,600
50	6,000	0	4,629	50,923
55	6,000	0	11,119	122,306
60	6,000	0	21,570	237,268
65	6,000	0	38,401	422,416

Without the benefit of a Keogh, poor Mr. Dim immediately had to pay $2,340 (39% of the $6,000 he put aside for retirement) in taxes so he began his investment program behind Mr. Bright who was always able to invest the entire $6,000 he chose to put aside without its first being subject to taxation. On top of this all the interest Mr. Dim earned was taxed each year at the 39% rate the end result being that Mr. Bright had $265,332 more than Mr. Dim to ease his retirement years entirely thanks to his Keogh Plan.

Perhaps you should try to qualify! If you are self-employed in even a part-time business as long as you don't incorporate you may be eligible. It's worth discussing with your attorney or other adviser, don't you think?

IRA- INDIVIDUAL RETIREMENT ACCOUNTS

In 1975 IRAs were available to employees whose companies did not have a retirement or pension plan they could join. Thanks to the ERTA (Economic Recovery Act of 1981) now every working person can each year put $2,000 into a tax-deferred IRA. The only requirement is that the income be earned, i.e. a salary as opposed to interest, dividend or legacy income. The beauty of the IRA is the chance to have interest compounding over time with no taxes due until the money is withdrawn.

Most accounts are opened by people in the 45-54 age group but an IRA is the best deal for those in their twenties because the further you are from retirement the more the IRA's tax-deferred compound interest can do for you. For example: if X opened an IRA at age 25 and began investing $38.46 a week (within the annual allowance of $2,000 for a single person), at 12%

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compounded annually he would have $1,718,285 by the time he was 65 years old. That's the miracle of compounding over a forty- year period!! If on the other hand, Y waited until he was 50 years old to open his IRA, even though he were to make the same contributions of $38.46 a week at 12% interest compounded annually, by the time he was 65 he would have $83,507. Not to be scoffed at, but still the advantage of starting early cannot be overemphasized when it comes to tax-deferred compounding. (Remember Mary and Sue in Chapter Fifteen?) Of course, inflation may put a damper on your expectations of what being a millionaire will mean in 40 years. It may well be that bread will cost over $100 a loaf! But even although you may not live like a king, thanks to your IRA you may be able to remain at your pre retirement level of comfort without the sacrifices retirement so often entails.

If only one spouse works, the couple together can contribute $2,250 but there must be a separated account opened for each spouse and the $2,250 can be divided any way you choose; half in his account and half in hers as long as no account has more than $2,000 contributed in any one year. it is not necessary to contribute every year nor is it essential to contribute the full $2,000 or $2,250 -- any amount up to that is fine. If both spouses are working then each is allowed to contribute $2,000 to his/her own account which is really a total of $4,000 a year per couple.

Some companies have payroll plans where so much is automatically deducted from your pay check and put into an IRA. This is an excellent way for someone to save who otherwise would not have the discipline to do so. It is relatively painless and very convenient.

The IRA fund must not be disturbed until you reach age 59 1/2. If money is withdrawn before that time there will be taxes due on the amount withdrawn plus a 10% penalty. However, IRA funds may be transferred from one qualified institution to another as often as you wish with no penalties. If you wish to move the funds yourself they must be placed in another IRA account within 60 days or the above mentioned penalties will be assessed. Moving the funds yourself rather than having an institution arrange the transfer is called a "roll-over" and only one "roll-over" is permitted each year. Uncle Sam has not forgotten about his share of all that money accumulating in your IRA and to make certain he gets his share you must start withdrawing your funds when you reach age 70 1/2 . The withdrawal can be made all at once in a lump-sum, in which case Uncle Sam is right there to levy taxes on the entire amount. At any rate there is a minimum amount which must be withdrawn when you reach 70 1/2 and on a schedule which according to actuarial tables would assure the depletion of the fund during your life span. Of course, the amounts withdrawn can be reinvested in any number of entities but not another IRA. Failure to withdraw the proper amount results in a penalty equal to half the amount you should have withdrawn.

In spite of these stiff penalties, which you should take care to avoid, an IRA is an extremely good investment. You can open IRAs at banks, savings and loans, credit unions, brokerage houses, mutual funds and insurance companies and also at some work places. You cannot invest in precious metals, life insurance or collectibles, but that leaves bank certificates, money-market funds, bond annuities, treasury notes, real estate limited partnerships, stocks, mutual funds, and many, many others; a pretty wide choice. However, like the purchase of life insurance when there are numerous choices it is time for self-analysis, preferably with some professional help. I

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will attempt to give you briefly some guidelines. Your own personal objectives will depend on your age, financial circumstances and temperament.

If you prefer a place free from worry and decision making, look into a bank, savings and loan or credit union. They have professionals managing the funds and your account is insured by the government up to $100,000. Make sure you open another IRA whenever the $100,000 mark is reached with any one account so you will get the complete government insurance coverage. You can have as many IRAs as you want just as long as you do not put more than $2,000 of newly earned money in the combination of all the accounts in any one year- you can transfer any retirement funds (old dollars) you want. The only decision that must be made is whether you will choose a fixed or variable interest rate. You should consider a fixed interest rate only if you feel interest rates will fall during the term your funds will be "locked in". That way you will be assured of the high rate of return you anticipated when you invested your money, for a 30 month term, for instance.

The only meaningful way to comparison shop is to request the effective annual yield. Interest is compounded in many ways; yearly, quarterly, monthly, weekly or daily. for instance, a simple (not compounded) interest rate of 14.375% might yield the same income as a 13.25% rate which is compounded daily. The effective annual yield is very important so shop carefully. Don't open an IRA any place where they won't tell you the annual effective yield.

The main drawback to opening an IRA with a bank of savings and loan, is that if you should need to withdraw your funds for an emergency there are heavy withdrawal penalties. These penalties are on top of the taxes which become due on withdrawals and the IRS 10% penalty.

Even though money market IRAs are not insured they are relatively secure, especially if invested in treasury bills or government bonds, Not only can the account be moved around without penalty, but the charge to manage your IRA in a money market would only amount to about $10 per year.

With a mutual fund group you can speculate and if you are young enough, afford to make some bad judgments knowing you have the time to recoup any losses. The advantage here for someone who has or wants to acquire the skill and has the time and temperament is that you can switch the funds as the economy and your own personal finances change. You avoid getting locked into one type of investment by joining a large fund group with ample diversity. In a no-load fund you deal directly with the company or transfer agent with no commissions involved as opposed to a load fund where shares are sold through a broker who charges a commission.

An insurance company IRA is an annuity and you must weigh the safety, fees involved and investment potential carefully.

You can always open a "self-directed" IRA but it must be with a brokerage house as you must have an IRA Trustee. The only people who might want a self-directed IRA are professional investors who believe they cold handle the investment funds better than any other manager. However, they would be faced with high fees in the form of commissions and, of course, the

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energy and time involved in self-managing the funds rather than leaving that to professionals employed by the other IRA institutions.

In the final analysis, however, you cold find that an IRA is not right for you! If you have only limited funds you must choose what to do with your savings dollars and it could well be that a savings plan where you work could be the best idea. If the company matches more than 25% of your contribution then even if the savings is accomplished with your after-tax dollars you would be ahead of the typical IRA. Remember brokers and financial adviser don't get commissions by recommending your company's savings plan. Look out for yourself!

MUNICIPAL AND OTHER TAX-EXEMPT BONDS

The final alternative to an IRA is open to everybody; municipal and other tax-exempt bonds and funds. Of course, they pay less interest than the taxable investments but they are great if you are in a high enough tax-bracket so that being tax-exempt weights the investment. This type of investment might be a winner if you are pretty certain to withdraw the savings before age 59 1/2.

SUMMARY

Many pensions plans today are money-purchase or target plans where the ultimate benefit to the participants depends on investment experience. Consider yourself one of the lucky ones if yours is a defined-benefit pension plan.

Because business has been "off "the last few years, profit sharing plans have not been very attractive. In many instances, management struggled heroically just to keep employees on the job without worrying about sharing non-existent profits. Still the fact that benefits are permitted to be withdrawn or borrowed against after only two years participation in a profit sharing plan is an intriguing feature of such plans.

The various stock ownership plans, deferred compensation plan, specialized TSAs and Thrift plans all have their good and not-so-good features. The best ideal of all is to have an IRA and the tax exempts and company or Keogh plans if you have that much money you can just put aside for savings. Most of us have to make a choice because we're lucky to be able to get $2,000 each year that isn't sorely needed for creditors or necessities currently. Just remember you can have an IRA and these other plans if you should ever have more than $2,000 to save. Never, never again think of the old piggy bank or pass book savings account when there are so many place to let your money work for you! The laws are changing constantly and the ceilings and rules applicable in 1982 will be outdated in 1984 in some instances so do your homework (books again) and if anything isn't crystal clear consult a professional.

If you are an employee, the main thing for you to remember is that ERISA (although in my opinion it may have wounded the geese that lay the golden eggs) was enacted for your benefit. You should be able to get from your pension plan administrators a special summary of your retirement plan in easy-to-understand language. Armed with this information tackle the worksheet which follows.

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The world may be your "oyster" but it's up to you to pry it open!

Worksheets - Chapter Sixteen
What You Should Know About Your Employment-Related Retirement Plans

This will take some research on your part but the answers to these questions will simplify your planning in this area. Write all the information you come up with in your notebook.

1. How many years on the job are required before you qualify for a pension?

2. Will the time you put in before the plan was initiated count towards determining the number of years worked?

3. Can these years be cumulative (leave or lay-offs OK) or must they be continuous years worked?

4. How long do you have to work each year to have the year included as credited service?

5. Is there an age requirement?

6. How do you apply for benefits?

7. How are your benefits determined?
fixed amount?
number of years worked?
amount of compensation received
combination?

8. Are you obligated to contribute a part of your salary to the plan on an annual basis?

9. How much will the employer contribute? Does the contribution involve your savings as well as the company's profits?

10 Can you invest the savings and the company's contributions in different types of investments? Company stock? A portfolio of growth stocks or long-term bonds?

11. Are you able to withdraw the full value of your own savings and the accumulated income whenever you want?

12. How long must you wait until you can withdraw your portion of the company's contributions? Are you penalized for withdrawals? Must you wait until you leave the company?

13. What are your benefits if:
job terminated now due to lay-off, fired or company bankruptcy?
you change jobs now?

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you become disabled?
you retire early?
you reach retirement age?

14. Are benefits tied in some way to cost-of-living? How?

15. Is your plan insured? Fully?

16. Is your plan integrated with social security? What is the formula?

17. What kinds of survivor's benefits does your company offer? Can your beneficiary receive benefits guaranteed until his or her death?

18. Is it necessary to give up a part of your normal pension in order to receive survivors' benefits in case of your death?

19. Must you opt for survivors' benefits before your retirement? How long before retirement must you choose?

20. What benefits are available to your beneficiary if you die before retirement?

Recommended Reading
Chapter Sixteen

The ABCs of IRAs, by William Grace, Jr.
*Everything You Should Know About Pension Plan*s, by Fay and Leo Young
You & Your Pension , by Ralph Nader and Kate Blackwell
The Coming Revolution in Social Security, by Haeworth Robertson
Social Security & Pensions in Transition, by Bruno Stein
Social Security: The Fraud in Your Future, by Warren Shore
Policy Making for Social Security, by Martha Derthick
Social Security Overpayments, by Peter Trozan
Social Security, by Robert J. Myers
The Complete & Easy Guide to Social Security & Medicare, by Faustin Jehle
Your Complete Guide to IRAs & Keoghs, by Jack Egan

Write to: The Pension Rights Center
1346 Connecticut Avenue N.W.
Washington, D.C. 20036

Chapter 17
How to Take Benefits

In chapter seven we discussed the various ways to receive insurance proceeds. Proceeds fro pension and other retirement plans require the same type of analysis and involve many of the options faced in chapter seven.

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Many people, in an attempt to provide for a spouse, choose to receive the smallest amount of income while they are living, with the expectation that they will die first and there will be more financial security of a loved one. What happens if the spouse dies first? You are stuck with lower payments than you are entitled to and the company is the winner.

In a majority of cases it would be better to take the "extra"(difference between high and low pay out options) and buy a term life insurance policy with a portion of it to provide for the surviving spouse. In that way, even if your spouse dies first, you are still entitled to the highest (100%) pay-out and on his or her death you can simply cancel the term policy on your own life.

Of course, one valid reason for taking less than 100% of your pension might be the fact that your are uninsurable and your spouse has no other protection (not a very common situation).

Under ERISA (employee Retirement Income Security Act) the normal annuity form is at least a joint and one-half survivor annuity unless the covered employee does something about it. I you want a single life annuity you must elect it under the rules set forth in your pension plan. Just consider the following example before deciding.

SINGLE LIFE ANNUITY

Xavier and Yvonne, both retired from their jobs and elected to take 100% of their benefits with no survivorship rights. Xavier was entitled to $500/month or $6,000/year and Yvonne was entitled to $400/month or $4,800/year. They drew pensions for ten years receiving a total of $108,000 in that time.

JOINT AND ONE-HALF SURVIVOR ANNUITY

Abigail and Bruce were co-workers of Xavier and Yvonne and retired at the same time but decided to take the 50% payment with survivor benefits. Abigail was entitled to $500/month or $6,000/year and Bruce was entitled to $400/month or $4,800/year but they each received half or together $54,000 over a ten year period.

At the end of the tenth year Xavier and Abigail both died. Yvonne received $400 instead of sharing the $900/month as before, while Bruce continued to receive $450 as always. Bruce and Abigail both died at the end of another five years. Their respective benefits from the company had been.

	Yvonne	Bruce
1st 10 yrs.	$108,000	$54,000
next 5 years	$24,000	$27,000
	$132,000	$81,000

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A study of the opposite page will show that even though both couples are entitled to the same pension dollars, Xavier and Yvonne, who chose the pure annuity, came out ahead in this example.

HOW DISTRIBUTED

LUMP SUM

A lump-sum distribution must be made within one year and must consist of everything the employee is entitled to with no credit remaining in the plan. The portion attributable to the employee's pre-1974 (ERISA) service is taxable as long-term capital gain. The part due to services from 1974 on is taxed as ordinary income. It can be divided by ten and then have the applicable single-individual rate tax table applied (even if the employee is married with dependents.) The resulting figure is then multiplied by ten to find the tax. The Tax Reform Act of 1976 gave the participant a new election to treat both portions, pre-as well as post-1974, as ordinary income subject to the ten-year-averaging formula. This gets more complicated than I have stated and is something to bring up with your accountant. Where contributions are made by an employee they are made with after-tax dollars and are not therefore taxed again upon distribution. If the distribution is made to a sole beneficiary, upon the employee's death there is a special employee death benefit you should be aware of. The first $5,000 of the otherwise taxable benefits are received by the beneficiary free of all taxation.

If the proceeds are to be kept out of the deceased employee's estate (free of federal estate taxes) the beneficiary must have the tax advantages normally accorded such a lump-sum distribution, namely capital gains treatment and ten-year-averaging. the choice of having the proceeds taxed as ordinary income but kept free of estate taxes or having the ten-year-averaging and capital gains advantages applied to the proceeds and subjecting them to possible estate taxation, can only be made by analyzing each individual case to determine which election would result in the greatest tax savings. Any death benefits attributed to the employer's contributions are not included in a deceased employee's estate. More will be said about estate taxation later.

If you change jobs and receive the pension benefits that you are entitle to (vested) from your old job, you can keep them and do what you like with them but they are taxed as ordinary income during the year received with no special treatment allowed. If you want to avoid such taxation, you can, within sixty days of receipt, reinvest the process in an IRA account without tax consequences. This is called a "roll over." Partial roll overs are allowed with means you can keep and be taxed on a portion of the distribution and reinvest the rest within the sixty day limit.

ANNUITY

Annuity distribution is a term applied to all ways of receiving benefits other than in lump-sum. Inflation prior to 1983 wreaked havoc with the purchasing power of retired persons receiving payments from a fixed dollar annuity so new variations of the fixed annuity were developed. Some plans attempted to tie annuities to some sort of price index so the purchasing power of the retiree would remain relatively constant. The variable annuity plans have the same goal and attempt to win their battle over the erosion of the pension dollar by investing pension

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contributions in a segregated portfolio for equity securities; the idea being that these is a correlation between the cost of living and the other equity investments. Of course, the possibility of greater growth is accompanied by greater risk and possible loss of capital.

Your premium dollars purchase "units" whose value fluctuates with the market. Therefore, you, as annuitant, assume the investment risk when purchasing a variable annuity but the company is guaranteeing that you will not outlive your income in terms of annuity units; it's just that those units may not be worth enough to live on! On top of this, insurance companies charge sales fees, sometimes up to 8% of each contribution, and management fees usually totaling 1/2 to 1% annually of the fund's net asset value.

In non-contributory plans, since the employer has contributed untaxed dollars to the employee's account, on distribution all the annuity payments will be taxed at ordinary income rates. The rules are rather complicated where contributory plans are concerned. Basically, the person entitled to the annuity figures the ratio of his investment in the plan to the anticipated return from the plan and excludes a like proportion of every annuity payment from his gross income. This is refereed to as the exclusion ratio. Your accountant or other tax professional can give you more details.

There is a simpler alternative though. If an employee in the first three years, receives an amount which is the same or more than his investment in the plan, he can exclude those payments from his gross income. Then, beginning with the fourth year, he simply treats all of the future payments as gross income.

PROS AND CONS OF ANNUITIES

Annuities are a gamble that you will outlive your resources. If you have acquired a significant amount to work with and are a prudent investor, it is a gamble that would be hard to win. For example, if you invested $100,000 at 10% you could pay yourself $10,000 a year indefinitely. The withdrawal would equal the income earned and the capital would constantly remain intact. (Of course, I am using a fairy-tale would of no taxes!) If you were to raise the disbursement to yourself without increasing the earning power of your principal at the same time, your reserves would eventually dry up. But even by increasing your spendable proceeds by $2,000 a year ($10,000 to $12,000) the principal would last for eighteen years! On the other hand, if you were to keep your requirements steady at $10,000 a year and were able to obtain better than a 10% return on your original capital of $100,000 your principal would begin increasing each year.

WHEN DOES DISTRIBUTION TAKE PLACE

Distribution can occur at normal or early retirement, when the employee changes jobs, is disabled or dies or if the plan itself is discontinued. Additionally some distribution can occur during an employee's illness, to pay medical expenses before or after retirement and even during periods when the employee is laid-off.

Disability causing premature retirement is planned for in some pension plans. There are various options: The disabled, under one option, can retire at an actuarially reduced level; another allows

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for a kind of severance pay based on a percentage of an employee's past earnings; or pension credits can continue to accumulate with the passage of time as if the employee were still on the job and his full retirement benefits would begin at normal retirement age.

SUMMARY

As you may have guessed, I do not favor annuities, even the "new improved" kinds. However, I'm sure your insurance agent will make a good case for the other side. Therefore, with an awareness of my own bias and from a sense of justice I recommend you discuss the subject with your agent before making any decisions. Remember, to ask yourself just what personal interest the advisor may have in your decision; will he stand to gain if you decide one way or the other? In the long run, it's all up to you. You may find it helpful to post the following sign seen in a New York cafeteria on your desk or wall: "Courteous and efficient self-service."

Worksheet - Chapter Seventeen

HOW TO TAKE BENEFITS

Read each statement and put a true or false after it.

1. In my family several members have lived past the age of seventy?_____

2. I don't mind the sales and management fees which accompany some

annuities._____

3. My retirement plan is a contributory plan._____

4. I don't want responsibility when I retire._____

5. I expect to live beyond the normal life-span._____

6. I am uninsurable._____

7. I don't think I could invest my money to keep ahead of inflation._____

8. My spouse is not the beneficiary of any insurance on my life._____

9. I like to feel I am being taken care of._____

10. My spouse has no independent assets._____

11. I don't like to manage my own investments._____

If you answered with a TRUE in nine or more cases annuities are right for you.

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If you answered with a FALSE in seven or more instances consider taking the proceeds in a lump-sum and investing for your own account.

If you came out somewhere in the middle ask some more questions, do some reading and give your circumstances a little more thought.

Recommended Reading
Chapter Seventeen

Money for your Retirement, by John Barnes
Personal Financial Survival, by Brownstone & Sartisky
Inflation Proofing Your Investments, by Browne & Coxon
Can We Afford Early Retirement? by Frank Kleicler
*Your Retirement Inco*me, by James Jorgensen
Personal Financial Planning, by Amling & Droms
Money & Retirement, by LeClair-Leimber-Chasman
The Star Spangled Retirement Dream, by James Gollin
Creating Promise Out of Threat, by Robert Kinzee

Chapter 18
Older Achievers

This chapter has nothing whatsoever or everything to do with retirement planning, depending on your pint of view.

One of my dearest friends is in fairly good health as she nears the century mark but for several years she has shown little interest in living. Usually when that occurs psychologists tell us a person's health deteriorates and they do in fact die. The mental outlook of my friend has not seemed to harm her health at all but of course worries those around her. One obvious conclusion is that her true feelings are very different form her words. Nevertheless, it is hard for all of us to see people who have been active achievers in their younger years let themselves vegetate in their old age. I believe many people think they are supposed to be "through", "worn out," retired at a certain age. We tell them that continually in a thousand subtle ways. From our earliest years we are used to getting our idea of ourselves through reflection from other people. Even though we say it doesn't matter what others think of us, our actions belie that assertion.

By making retirement mandatory, establishing quiet secluded retirement communities, providing basket-weaving classes and other nursery school activities and labeling it recreation we are telling our older people what we think of them.

Today one out of every five American is over 55. Other cultures honor their elderly for their experience and wisdom. We in the United States, in our exclusive worship of youth, are wasting a vital resource by fostering the attitude that the old must inevitably be a drain on our society. The helpless infants and youngsters we are willing to support because they are our future, but when the old are lumped in this same "helpless" basket there is often resentment. Perhaps that is

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because hoping for something (a better future) is a stronger emotion than owing something (a debt for what parents, teachers and our elders have done for us in the past.)

Elderly people can more than carry their weight and if you already know this you can skip ahead, for in this chapter I intend to show just that with illustrations of older achievers.

The first three people I mention because I have a personal connection to them. None would be able to say they know me but I remotely know them. Two because they live near me and Professor Hildebrand because I have been to his house on several occasions back when I was in junior high school and his granddaughter was my best friend.

INSPIRATIONS FROM THE 1980S

JOEL HILDEBRAND

Joel Hildebrand was a professor of chemistry at the University of California in Berkeley, where he authored a freshman chemistry text that was used by thousands of students over the years. On the occasion of his 100th birthday the University held a week long celebration. I am not mentioning him to eulogize him as to point out his connection with the ordinary man. Of course, one of the reasons I chose to mention Joel Hildebrand was his age and the fact that the was still active, interested and productive past the time when that is considered ordinary. The other reason is to illustrate the fact that one needn't be a politician or a celebrity in order to affect people. A professor of chemistry at one of the most prestigious Universities in the world is not exactly the ordinary man but he was remembered most by his students for his humanness and that is something to which we can all aspire.

Since I began this book Joel Hildebrand has died. His is an example of what I mean to convey in Chapter Fifteen when I spoke of no one knowing if he has really led a good life until the end comes. The end of Joel Hildebrand's life came when he was still an active, interesting and greatly admired and appreciated gentleman 101 years old and it was good!

EDITH TRUESDELL

A little close to home is the example of Edith Truesdell, a 94-year old artist who lives not far from me in Carmel Valley, California. She recently (1983) had an art exhibit in Monterey and among the paintings shown were three which had been completed during the past year.

ANSEL ADAMS

An even closer neighbor is Ansel Adams whose photography is known worldwide. His creativity has brought pleasure and a new way of looking at things to many people. He gives speeches frequently and livens up any number of groups just with his illustrious presence; willing, active and rarin' to go!

ESTELLE WINWOOD

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Estelle Winwood has been an actress for eighty-five years, since she was fifteen years old. Not long ago she appeared in a guest spot on a a television series ("Quincy"), and was seen in a movie as recently as 1976 (Murder by Death). When asked on her hundredth birthday if she was still active in her profession she replied she was open to offers. I only hope someone has a current role for her. Where else will they find an actress with eighty-five years experience?!!

HELEN HAYES

Another great lady of the theater, presently in her eighties, is active in a myriad of projects. Helen Hayes hates the words aging, elderly, or senior citizens. She refers to "her generation" as "grandpersons". She points out that the attitude of people in the theater is unfortunately not common to the rest of society. So many great roles are written for older character actors. Grandpersons have a place in the theater, in fact they are needed. There is no thought of forced retirement in show business. Once you start listing entertainment celebrities who are past eighty there is no stopping. I think the healthiest thing they all have going for them is that they are recognized and cherished. So many people care about them that a good self image is constantly reinforced. In contrast, often the elderly (grandpersons) are quite alone without family or friends with nobody who knows of their past accomplishments and experiences nor is willing to listen.

JAMES MICHENER

James Michener, who is still approaching his eighties (75) is one of my personal heroes. Born without the love and security of a natural family, he is one of those rare people who goes through life making lemonade from lemons. He worked hard for his achievements but never ceased to share the accolades with others; especially the American system which he lauds for making his successes possible. He is even now working on a novel about Texas which is slated for publication sometime during his 78th year and he reportedly has ideas for at least half a dozen more books. I for one look forward to them all.

ARTHUR MURRAY

Time Magazine recently referred to Arthur Murray, 87 as one of the oldest money managers in the United States. Most of us, at least those of us over thirty five, immediately recognize Arthur Murray as the founder of a national chain of dance studios. *Time's* identifying him with a new career startled me and makes him a perfect illustration of what I am trying to convey about older people. They're not through until they, or society, call it quits. I'm not claiming one of the brokerage houses or financial planning firms would have hired an 87-year-old man as a consultant (they'd probably all love to now that he has proven his worth.) Only because he had his own funds as well as those of trusting friends was he able to prove that he could do a superior job of investing.

APPY KROLL

According to a report issued by the Census Bureau in the summer of 1983, of the 232,057,000 people in the United States, 2.4 million are over age 85. Included in this group are 32,000 people over 100 and one is Appy Kroll, at 106, the oldest grandperson mentioned here. We would not

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know much about Mrs. Kroll, as she is less of a celebrity than the others I have mentioned, if it were not for her longevity which has recently brought her into the limelight. She lives in Spokane, Washington with her 80-year-old son and is remarkable because at her age she sounds like the "mom" next door. She stays active, cooks and enjoys music and is not letting her age dictate how she should live. I know of so many cases where well-meaning children have urged a grandperson to sell their home and go where they will be taken care of in case something should happen. The main motivation being the number of years the person has lived, not that they are in poor health or unable to care for themselves. Actually it is insurance for the younger person's peace of mind and often hastens the deterioration of the parent who listens. Hooray for Appy Kroll and her son Bill Schluter who know how to live!

GRACE MURRAY HOPPER

I read about Grace Murray Hopper in *Forbes* magazine in the summer of 1982. Not only was this lady featured as the oldest officer in the active duty in the Navy, a Captain at age 75, but she was engaged in a crusade to get businessmen, students, and others into the "new generation" of computers!! Endowed with remarkable intelligence and curiosity that won't quit she is the creator of the computer language called COBOL (Common Business Oriented Language). She is proof that no matter what "they" tell you creativity thrives in grandpersons as well as the young!

RUTH ROCKFARB

Ruth Rockfarb, a tiny woman weighing only 100 pounds and less than five feet tall, was recently featured on a television show. In spite of the warnings of well-meaning "friends" who were sure she would suffer a heart attack, this lady started running at age 72. now, almost ten years later, she has participated in three marathons (26 miles) and has always finished every race she entered. Instead of letting age dictate her activities, Ruth Rockfarb discovered a new interest in life that not only afforded new friendships but also served as an inspiration to others.

CLARENCE ROSS

Clarence Ross at 83 keeps winning swimming meets. He keeps body and mind in shape with his keen interest and sharp competitiveness. Sports are good for people of all ages and it's never too late to find one you're good at and can enjoy.

SENATOR SAM ERVIN, JR.

Senator Sam Ervin, Jr. is more than a political figure (now a lawyer again in North Carolina), he has become to some over the years a folk hero approaching Will Roger's fame. I include him here not for all his witticisms and persuasive stories or his insight into our country's ills, but for a statement he once made that should be taken to heart by everyone who reads this chapter. When asked how he wanted to be remembered he replied he didn't want to be remembered too soon. We all know of people who even while technically still living, are memories all too soon!

INSPIRATIONS FROM HISTORY

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Titian painted his masterpiece, *The Battle of Lepanto,* at the age of 98. Verdi wrote his great opera, *Othello,* at 74, and *Falstaff* at 80. Sir Isaac Newton, thought by many to be the most influential man who ever lived, was creative well into his eighties. Sir Christopher Wren retired from public life at 86; after that he spent five years in literary, astronomical and religious pursuits. Benjamin Franklin was in his seventies when he was sent to France in 1776 to strike an alliance between the two countries (France and America). The famous French criminologist upon whose life the *Count of Monte Cristo* is based, solved his last criminal case when he was 80. Thomas Hobbes published his translation of the *Iliad* when he was 88. Emmanuel Kant wrote his *Anthropology* at the age of 74. Thomas Edison built chemical plants after he was 67. Elihu Root, at 84, reconstructed the World Court. General Douglas MacArthur was supreme commander of the occupation in Japan while in his seventies. At age 85, Bernard Baruch, adviser to six American presidents, was able to say: "Always the thought of tomorrow has buoyed me up. I have looked to the future all my life. I still do."

Each day and every day of your life you are storing up experiences. The first 40 or 50 years you are primarily a "taker", the last 50 years should be for giving. It is time for society to acknowledge the wealth that has accumulated in our senior citizen pool over the years in terms of observations, skills and practical experience.

Worksheet - Chapter Eighteen

Be on the lookout for older achievers. They are everywhere.

Look among your own family ancestors as well as those living.

How many movies depict accomplishments of older people? Gandhi and Winston Churchill are two notables.

Look for news about the older generation in television spots.

Your local newspaper is a good source of what good things "grandpersons" are doing in your own community.

Make your own list of at least ten people who have made notable contributions to society after the age of 65.

Try to encourage an older fiend or relative to participate in college courses or physical activity to try something new each year.

Remember these words attributed to Maurice Chevalier: "growing old isn't so bad when you consider the alternative."

Recommended Reading

Chapter Eighteen

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The Graying of America, by James Jorgensen
Over 50, by Aren Uris
The Rights of Older Persons, by Robert N. Brown
The Other Generation Gap, by Cohen & Gans
The Graying of Working America, by Sheppard & Rix
The Retirement Money Book, by Ferd Nauheim
Your Money & Your Life, by C. Colburn Hardy
50 Plus Magazine

Section Five
Tax Management

Chapter 19
"SIR" Social Security, Income and Real Estate Taxes

THE INCOME TAX

It may be an understatement to say that our tax law is complex; in fact, it is almost laughable when you consider the enormous mass of instructions, regulations and contradictions which make up the Internal Revenue Code which affects the life of every citizen in one way or another. There are currently 2.350 pages of Internal Revenue Code, 5,600 pages of official Regulations, 24,500 Revenue Rulings, 37,000 Tax Court and Board of Tax Appeals Rulings, 35,000 Federal Court decisions and currently pending rulings, regulations and propose new legislation as well. The main thing to remember is that the people with the greatest understanding of our tax laws generally end up paying the least taxes.

INCOME

Do you know what income is? If you're wise in the ways of our tax codes you'll ask: Do you mean gross income, adjusted gross income, ordinary income, earned income or taxable income?"

Congress defines gross income as "all income from whatever source derived." That doesn't seem to leave much to the imagination; salary, dividends and earned interest, proceeds from sales, services, barter proceeds, alimony payments, pension and other retirement plan payments, winnings (prizes as well as dollars), anything you find, canceled debt (you may not get money but you get relief from no longer having to pay it), and so on and so on. Now that you're properly convinced that everything you can think of is income, I'll tell you about the exceptions.

GROSS INCOME

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Not included in gross income are life insurance proceeds which are though to indemnify a beneficiary for the loss of a loved one and perhaps someone who was also a means of support.

Damages received because of personal injury settlements are excluded from gross income for the same reason; they are viewed as indemnity for pain and suffering; also excluded are medical expense payments made by your life insurance company. An added bonus here is the amazing fact that the lost earnings which would have been taxed if received as wages are free of all taxation when obtained because you can't work!

As mentioned briefly in chapter seventeen, the first $5,000 of death benefits from a deceased spouse's employer is excluded from your gross income.

Disability payments from insurance you purchase yourself are not included in gross income but if your employer paid for the contract and you did not report those employer-paid premiums as income then generally the disability payments will be considered taxable income to you.

Workmen's Compensation benefits are not included in figuring your gross income.

Salaries of enlisted men in combat zones are not taxed, and officers get the first $500/month excluded.

The values of gifts are also excluded. the rationale seems to be that the givers of fits are the ones with the money so tax them. An exception to this rule is the case where the gift you are given consists of the income from real estate or the right to receive interest or dividends from bonds or stock while the donor continues to hold the property itself. Since the rents, interest or dividends are new income they haven't been taxed already (in this case the donor hasn't paid the tax) so the IRS comes after you , the donee.

Meals and lodging are excludable if essential to your job,

The value of ministers' living quarters are also excluded.

Scholarship and fellowship grants are also excludable when applied toward study and research as opposed to teaching. The rationale here is gifts are untaxed and compensation (wages form teaching) is taxed.

The first $100 ($200 for joint returns) of dividend income is excluded from gross income each year. After all, the corporation has paid taxes on it once already.

Beginning in 1985 taxpayers can exclude from gross income 15% up to $3,000 ($6,000 for joint returns) of "net interest" earned. "Net interest "means you can deduct interest paid for any reason from that received from investments and pay tax on the remainder if it exceeds $3,000.

Living expenses paid under a homeowner's policy if your house was damaged and you have to live somewhere else for a while are also excluded from gross income.

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Social security benefits and mustering-out payments from the armed forces are both excluded from gross income.

The whole subject of fringe benefits and barter are in limbo. The IRS wants to include them in gross income but by their nature they are hard to trace.

Term life insurance premiums paid by an employer are not included in an employee's gross income unless and to the extent that the face value of the policy exceeds $50,000.

Unemployment compensation is taxable only if and when your total income exceeds $20,000.

Since an annuity is purchased with dollars which have already been taxed, when you get those dollars back they won't be taxed again but what they "earned" will be. You'd think the politicians would let you recoup your capital before they begin taxing the interest you are earning; after all, you could die without having gotten back the original amount you paid for that annuity so it can't really be clear just what they are taxing. Since they can't wait or the real earnings to begin, they use actuarial tables to determine what you will or would have made if you live the amount of years you're supposed to. The insurance company will provide the actuarial information you need for your tax return.

You 're even taxed on interest from Treasury bills and bonds of the United States Government. You lend the government money, they give you a modest interest and then have the nerve to tax you on it! They figure your risk is zero but it still doesn't bring out one's patriotic feelings, does it? On the other hand, interest paid to citizens who loan money to state and local governments by purchasing bonds, is excluded from gross income.

At this point the IRS can see what you've got (gross income established) and it tries to control its appetite while you now proceed to take some deductions.

"DECs"(DEDUCTIONS, EXCLUSIONS AND CREDITS)

Before you get confused, let me arm you with three definitions which when committed to memory, should clarify many questionable situations. I call them "DECs": deductions, exclusions and credits.

Deductions reduce income.

Exclusions erase all memory of the transaction.

Credit reduces the amount of tax due.

We spoke of exclusions above in determining gross income. Now we will consider the role certain deductions play in establishing adjusted-gross income.

BUSINESS DEDUCTIONS

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Adjusted-gross income is really your "net income"; everything you make minus what you spent to make it, which I refer to them as "business deductions."

You may deduct from your gross income, with exceptions and explanations of course, all ordinary and necessary expenses connected with making a living. Commuting expenses to an from your job are not deductible , but any transportation expenses incurred while on the job are, including meals, lodging, transportation costs, tips, laundry, phone calls, etc. If you are an employee these expenses must have been incurred while "away form home" and IRS (Internal Revenue Service) defines "away from home" as requiring you to sleep or rest before completing your work. If you stay overnight you can then deduct meals, etc., but not otherwise. (One might suspect the sleep and rest requirement was a pet project of the hotel industry lobby." "Home" under this regulation refers to your principal place of business not your residence. You can readily see why it is important for a traveling salesman to establish an IRS defined "home" somewhere so he can be away from it in order to qualify for travel deductions!]

There is a great deal of litigation surrounding transportation and travel deductions so if you have such deductions in the normal course of your business be sure to read the publication IRS puts out describing its substantiation requirements in this area as well as those surrounding entertainment.

Entertainment expenses can only be deducted if you are a business owner or are an outside salesman unless you are reimbursed by your employer and can yourself substantiate the expenses (the burden is on you). You must keep an account book and provide receipts or other documentation for most expenditures.

Education expenses related to your trade or business are also deductible but not if the education qualifies you for a new job or career.

Moving is nowadays considered to be a cost of earning money if the move was made because of a new principal place of work. Once moved you must stay put pursuing a full-time occupation for a minimum of 39 weeks. Also our business must be at leas 35 miles (farther form your residence than was your old place of business.) There is no ceiling to the moving expenses you can deduct as long as they are legitimate, but there is a $1,500 limit for searching for new quarters. Otherwise you might look forever deducting your living expenses in some fancy hotel! Expenses incurred in both buying and selling a home are also included here up to $3,000 but remember your searching expenses come out of this $3,000.

Also deductible but not really business-connected are alimony payments and IRA and other retirement contributions.

PERSONAL LIVING DEDUCTIONS

In order to determine your taxable income the adjusted-gross income is reduced one step further by personal living deductions referred to as itimized deductions." These itemized deductions are: the interest deduction (whatever you have to pay for the use of someone else's money); the casualty deductions (losses of property caused by theft, fire , flood or other disaster); the

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charitable contribution deduction; the "medical expense" deduction: and the state and local tax deduction. Usually people in the higher tax-bracket choose to itemize; they often have large interest payments, more charitable contributions and they save more on every dollar than would an itemizer in a lower bracket. Under our progressive tax system as your income increases you get taxed a progressively higher rate.

The majority of taxpayers choose the "easy way" to reduce their adjusted-gross income; that is by using the "zero bracket amount"(standard deduction.) The zero bracket amount lets you automatically, no questions asked, reduce your adjusted-gross income by $2,300 if you're single, $3,400 for a married couple. You don't really subtract this amount from adjusted-gross income because it is figured out for you in the tax table, it is a built-in-deduction. Therefore, if you itemized you must immediately subtract $3,400 (on a joint return; $2,300 on a single) from your itemized deductions to counteract the forms.

EXEMPTION

Exemptions are another form of deduction; a people deduction. You reduce your income by $1,000 for each mouth you have to feed-- even your own. A mouth is considered yours to feed if you provide more then half of the support of an individual, thereby making that individual your dependent. Dependents include children under nineteen years; over nineteen if full item students (in school five months out of the year), or if they make less than $1,000/years; relatives who can live anywhere as long as half their support comes from you and they earn less than $1,000/year; non-relatives who must live in your house to be considered dependents but even so if your relationship is against the law they cannot be claimed as dependents (so far no live-in lovers, just spouses). As a rule the parent who has custody for the greater part of the year claims the child of a divorce as a dependent unless another arrangement has been reached.

SO AGAIN-- VAT IS INCOME TAX -- EH?

We started with the idea that everyone knows what income is: everything!! Then we erased a good portion of that income with a whole list of exclusions; that gave us our gross income. In order to arrive at our taxable income we had to go through three sets of deductions; business (things that help you make your living), personal (zero bracket or itemized deductions), and people (exemptions). After the first stage of deductions, when business oriented expenses were deducted from gross- income we arrived at what the IRS calls adjusted-gross income (net income). But it is only after the personal and people deductions are applied that your taxable income can be determined by referring it to the tax tables.

SOCIAL SECURITY

The Social Security Act was legislated in 1935 when there were fifty workers for every retiree. The tax was originally a mere one percent of an employee's salary matched by one percent from the employer. If these funds had been invested, as are the funds in all other regulated retirement plans, our social security system would not be in the financial straits it is today. In fact, one study showed if those finds had been managed and invested properly citizens could be receiving, with

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no strain, over triple the benefits the social security system is struggling to provide currently (1984).

Unbelievably, Social Security was an unfunded program; FICA taxes (Federal Insurance Contribution Act) have co-mingled in effect whith other funds for years instead of multiplying off by themselves as intended. Retirement benefits were simply paid out of current taxes, which was not too bad even in the 50s when there were sixteen workers paying-in current taxes fro every retiree receiving benefits. Today there are between two and three workers paying-in to every retiree withdrawing benefits and the tax is no longer one percent for employer-employee but over six and a half percent each with raises anticipated in the future.

Younger workers are justifiably bitter about the larger and larger bite social security is taking out of their pay checks. They come into the work place on the low end of the pay scale and find social security takes more from their generally meager wages than does income taxes.

The social security system is acquiring obligations faster than it is accumulating funds. That's not surprising when you realize the retired vote is the largest voting bloc in the United States and politicians have long realized the surest way to stay in office is to increase benefits for their constituents. Problems naturally arise when one Congress makes promises that a future Congress must keep. Over the years, benefits have spread to dependents and survivors so that barely half the beneficiaries of social security are retired workers who actually paid into the system. On top of that, other taxes will have to increase to keep up with spiraling benefits to retired state, local and federal government employees as well as retired military personnel.

Because social security trust funds are only allowed to invest in federal bonds, notes and treasury bill, large amounts of money are being drained form the private marketplace. Business, finding its after-tax earnings are insufficient to meet demands for expansion, is forced to borrow. Unfortunately most of the potential savings from Untied States citizens, which should be available for such borrowing, is removed from the system by the requirements of social security. From this scenario follows increased business obsolescence, unemployment and cries for "protectionism."

Social security is an example of government's attempting to accomplish worthwhile goals from a sense of compassion but overreaching itself to the extent that society ends up in a worse situation than before. A large part of the problem evolves from the inefficiency of such a huge bureaucracy which consumes 40% of what it takes in just to support itself! It is possible that sometime in the next twenty-five years payroll taxes may equal up to 25% of a citizens' wages. High social security taxes encourage both unemployment and inflation because the employer tends to react to his increasing burden by either hiring fewer employees or passing his inflated expenses on to the consumer.

Almost everyone has been concentrating on the possibility that our social security system might go broke. It is true that a handful of analysts have had the courage to point out what I believe to be the real problem that our politicians refuse to face; not that social security may go broke, but that social security may end up breaking our nation!

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REAL ESTATE

STATE AND LOCAL TAXES

There is no uniformity in the various state and local laws governing the collection of taxes. Assessments vary greatly from one locality to another. Judging solely on the basis of the amount of taxes residents are required to pay, it is obvious that some localities are far more expensive to live in than others. The fact that California is our most populous state and Alaska the least is proof (as if proof were needed) that people are not apt to base their decision of where to live on tax information.

On the other hand, most people don't bother to obtain such information and if they had it perhaps their decisions would be influenced. Certainly corporations are formed often on the basis of where the taxing policies are the most favorable. A large percentage, almost 75%, of all corporations are based in Delaware for that reason.

CALIFORNIA AS AN EXAMPLE

Proposition 13, the controversial measure passed by California voters in 1978, rolled back assessed valuations to 1975-76 levels and imposed a one percent ceiling on property taxes and also limited assessment increases to a maximum of 2% a year or the annual increase in the California consumer price index, whichever should be lower. In 1983 the sharp reduction in inflation was responsible fro the drop in California's property taxes to one percent. In addition to reforming California's real estate tax, Proposition 13 provided that non-property related taxes could only be imposed by approval of two thids of the voters. Although the United States Supreme Court held the proposition was unconstitutional over a challenge for ambiguities , it is these same ambiguities which are currently undermining Proposition 13's effectiveness as a buttress against higher taxation. the reference to "special districts," "special assessments" and "special taxes" is at the heart of the problem.

In 1982 a suit was brought by the City of Los Angeles Transit Commission (Commission) against George Richmond, its own executive director, for the specific purpose of clarifying Proposition 13's meaning regarding non-property taxes. The Commission levied a half-cent sales tax to raise revenue which the Board of Equalization (Board) refused to collect on the grounds that it was invalid under Proposition 13's two-thirds vote requirement. Finally the Board agreed to collect the tax if the Commission guaranteed to refund the money in case the tax was later judged invalid. Since neither the Commission not the Board were in a position to distribute refunds to millions of people (this half-cent tax was to generate approximately $225 million annually) the suit was brought by the Commission against its own director ostentatiously for a small infringement but purposefully to test the validity of the tax. The California Supreme Court evaded the question of whether the sales tax was a "special tax" by deciding instead whether the Commission was a "special district". The court found that the "special districts" alluded to in Proposition 13 meant districts that have the poser to levy property taxes and therefore because the Commission did not have such a poser it was not a "special district" and not governed by the restrictions imposed by Proposition 13.

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The two-third vote issue which the parties to the Los Angeles case had anticipated the court would tackle was actually decided late in the year in a San Francisco suit contrived in a similar manner by the City suing its own controller to get a quick ruling form the courts on the interpretation of "special taxes" as used in Proposition 13. The supervisors of San Francisco County extended a one-and-a-half percent payroll and gross receipts tax which should have expired in June of 1980. The controller argued "special" means extra or additional and that any new tax requires a two-thirds vote. The City, on the other hand, argued successfully that "special" refers to special purpose and since the payroll and gross receipt tax went directly into the City's general fund it was not "special" and therefore was not subject to the two-thirds requirement of Proposition 13.

The "special assessment" clarification was given by the courts in a suit involving a taxpayer in the City of San Gabriel, California, who fought a raise in his property taxes above the Proposition 13 limits. the increase was necessitated by the City's obligation to its employee pension fund which the court ruled was a contractural obligation which the City must be allowed to fulfill. According to California's Supreme Court Justice Frank Newman, if Proposition 13 had not provided for the fulfillment of prior contract obligations, such as the City's obligation to its employees, the entire proposition would have been judged unconstitutional by the Untied States Supreme Court.

It would appear that the California Court's interpretation of Proposition 13's ambiguous "special districts", "special taxes," and "special assessments" only served to open further the floodgate of higher and more taxes. Various citizen groups within the state continue to work on proposals to amend the controversial proposition.

In chapter twenty-one various taxing philosophies are discussed and many differing proposals explored. There are those of you who are practical and don't care how we (U.S.A.) got where it is today in terms of high taxes and higher budget deficits, and don't believe you can do anything about it anyway. You may just prefer to absorb practical information on minimizing the very real tax bite you personally must face. However, the best way you can work for yourself is to work for reform on a national level not just for reform on your own individual return. First, you have to decide what you personally think is right philosophically even though that may initially entail going against your own pocketbook. Things that are valuable always have a price tag!

Worksheet - Chapter Nineteen

1. Review the list of exclusions. Are you excluding all the following when you report your income?

life insurance proceeds
court - awarded damages
medical payments via insurance
lost earnings via insurance
1st $5,000 employee death benefits
living expenses via insurance while home was damaged
unemployment compensation (if total income is under $20,000)

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gifts
grants for study and research
annuity payments minus interest
1st $100 of dividend income
social security benefits
workmen's compensation
disability payment from personally paid insurance

2. Which of the following deductions are you eligible to take? Do they exceed the zero bracket limits??

- related to employment
- transportation
- meals
- lodging
- tips
- laundry
- phone calls
- education
- entertainment
- moving
- buy/sell home expenses
- alimony
- IRA (similar) contributions
- interest paid
- casualty losses
- charitable contributions
- medical expenses
- state and local taxes

3. Exemptions -- are you including everyone eligible?

minor children? elderly parents?
other to whom you contribute half their support?
no pets please!

Recommended Reading
Chapter Nineteen

The Complete List of IRS Tax Deductions, by Rosalie and Howard Minkow
Creative Tax Benefits, by Rosalie Minkow
You Can Profit from the New Tax Law, by Wiltsee and Sammons
How Anyone can Stop Paying Income Taxes, by Irwin Schiff
How to Pay Zero Taxes, by Jeff Schnepper
1983 U.S. Master Tax Guide, Commerce Clearing House
Travel and Entertainment: Business or Pleasure? Commerce Clearing House
1983 Guidebook to California Taxes, by Russell Bock
State Tax Handbook (all states) Commerce Clearing House
1983 Social Security Explained, Commerce Clearing house

Address: Commerce Clearing House, Inc.
4205 W. Peterson Ave.
Chicago, Illinois 60646

Consult the reading list at the end of Chapter Sixteen for information about social security taxes.

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Chapter 20
"PEAR" Postpone, Eliminate, Accept and Reduce

Tax evasion, dodging your obligation, may be a crime but tax management is not. Certain socially desirable investments are encouraged by the way our tax laws are written with provisions for the creative use of tax saving opportunities.

There are four ways to handle your taxes. they are easy to remember if you use the acronym P E A R; Postpone, Elimination, Acceptance and Reduction. I will, in this chapter, discuss each separately.

POSTPONEMENT

CAPITAL GAINS AND LOSSES

It is almost always desirable to postpone paying taxes whenever possible. (1) If inflation is a factor, your dollars will be less valuable in the future than currently; (2) you may find yourself in a lower tax-bracket, especially if you are about to retire. (3) the postponed tax dollars continue to work for you; (4) maybe your finances will take a turn for the better and you will be able to pay the taxes at a later date without resorting to borrowing; and (5) perhaps you will be able to take advantage of the capital gains provision in our tax law.

One basic tenet in tax management is to accelerate your current expenses and postpone income as long as possible. The reason for this has to do with the capital gains rules. We have discussed earlier the advantage of holding an investment more than a year so that upon sale the income will receive favorable tax treatment. Only 40% of the income (gain) will be taxed at your individual tax-rate as opposed to having a 100% taxed if the investment were liquidated before twelve months had elapse. Similarly if the investment produced a loss it would be either a short-term loss or long-term loss according to the same rules; i.e. whether it had been held over or under the twelve-month qualifying period.

Just as short and long term gains are taxed differently (100% taxable as opposed to 40% taxable), short and long term losses receive different treatment under current tax law. Short term (under twelve months) losses can be used to reduce ordinary income by 50%; it takes $2 of long term capital loss to reduce $1 of ordinary income. Naturally you would prefer to have short term capital losses if you must have losses at all.

REAL ESTATE

Real estate offers so many tax advantages it will be used as an example throughout this chapter. It is unique in that it can be used to postpone capital gain taxes indefinitely.

Any profit attributed to the sale of your principal residence need not be taxed until two years from the sale date. If during the period you purchase another home equal in value or more expensive than the one you sold, the gain from the first sale is postponed until you sell your new home at a future date. "Tax-basis" refers to the price you initially paid for the home plus

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remodeling expenses. Routine maintenance is not included but major improvements such as room additions, decks, patios, pool, landscaping, etc. are considered capital additions and raise your tax basis. It is possible to postpone taxation on probable gain in this manner over and over but each time the cost basis of the current home must be reduce by the amount of the deferred gain on the former home that means, of course, that your current home will be subject to a larger gain when sold. For example: Mr. John Dough, a taxpayer in the highest tax bracket, bought home "A" for $70,000 and sold it five years later for $90,000. Figuring the capital gains tax on the $20,000 profit, he would be faced with a $4,000 tax liability. Remember, according to the capital gains rules, only 40% of the $20,000, or $8,000, would be subject to taxation and at 50% which is the highest tax bracket rate currently = $4,000 Mr. Dough, however, doesn't pay that tax, he postpones it by purchasing home "B" within the two-year time limit, for $100,000. Three years later Mr. Dough sells home "B" for $150,000. His gain is $70,000 not $50,000, because his cost basis (price he paid for the house) is reduced by the amount of his deferred gain on the other house. ($100,000 price paid minus $20,000 gain house "A".) If we start with a cost basis of $80,000 it is easy to see how Mr. Dough is left with a capital gain of $70,000 ($150,000 minus $80,000 = $70,000). He can postpone paying tax on the $70,000 capital gain by buying another house valued at $150,000 or more and infinitum.

On the other hand, it should be noted that should a loss occur on the sale of your personal residence you could not deduct that loss from your taxes because it has no connection with a trade or business.

EQUITY INVESTMENTS

The capital gains concept favoring postponement of income holds for any equity investment with potential for appreciation in value. Precious metal, diamonds, art and other collectibles appreciate in value and are only taxed on their gain when sold. Of course, they pay no income until sold and may even be costly to hold because of the need for insurance, safe deposit boxes and other safety measures.

Common stock and discounted bonds are favorites in this area. Growth stocks are purchases with the idea that they will increase in value making them ideal candidates for capital gains treatment. When a bond is bought at a discount (less than par value) a gain is built in (difference between the price you paid and selling or maturity price), so if held for more than twelve months it will also be taxed at capital gains rates. But a word of caution: U.S. savings bonds are always issued at a discount but they are not treated as capital assets. The difference between the price you paid and the price the government pays you on redemption (or that you obtain from a before-maturity sale) is considered to be "interest" not a capital gain and is therefore taxed at ordinary income rates.

With series HH bonds interest is actually paid to the owner periodically and the owner is taxed as the interest is received. Series EE bonds allow you to pay taxes on an annual basis or postpone paying taxes until the bonds mature or are otherwise redeemed. Upon maturity series EE bonds may be exchanged for series HH bonds without triggering a taxable situation making the postponement of taxes even longer.

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EXCHANGES

Taxes may be deferred on simultaneous "like kinds" of property (Internal Revenue Code Section 1031). There are complex rules in this area for determining "like kind" and "fair market value". If in order to achieve a tax advantage, you are considering an exchange of property as opposed to an outright sale and purchase, make certain you contact a tax professional skilled in exchanges to guide you through the complexity of unique definitions and exceptions. Used personal property is an exception because it is unlikely you would have a taxable gain because the goods would have most certainly have depreciated below their original cost. However, real property and collectibles that have appreciated are given scrutiny by the IRS. New ruling are being issued continually and in favor of the taxpayer on occasion. Don't overlook the potential here for tax advantages but approach them armed with professional counsel.

RETIREMENT PLANS

In previous chapters we discussed in detail the benefit of having the investments increase in a tax-free environment. IRAs, Keoghs, life-insurance policies, employee benefit plans, deferred compensation plans, annuities, stock-purchase and profit-sharing plans are all examples of letting capital accumulate in a tax-free environment with taxation postponed until income is actually realized. Taxes are paid over time if income is taken in installments. If you elect to receive benefits in a lump-sum, ten year averaging softens the tax blow and is an excellent example of the rewards available to an astute taxpayer. Since 1976 it has been possible to receive your money all at once rather than in installments, and yet pay taxes as if it were distributed to you over a ten-year period. This can result in significant tax savings but there's a "catch" that may make you think twice before electing the ten-year-averaging treatment. This was mentioned when discussing lump sum distributions in Chapter 17..

ELIMINATION

Tax avoidance occurs when the rate at which taxes are saved by investing is greater than the rate at which taxes are paid when getting out of an investment!

Taxes can never be totally eliminated; there are just too many of them. If you made less than $3,400/year (at this writing) you might be exempt from the federal income tax but FICA taxes would come out of your wages and sales taxes would continue to be added to your purchases and so on. There is, however, one way of eliminating a tax completely, not just postponing or reducing it, but you have to know how and abide by the rules.

REAL ESTATE

Let's get back again to Mr. Dough. Suppose Mr. Dough is now over age fifty-five and decides to take advantage of another provision of the tax law as it pertains to real estate. There is a once-in-a-lifetime opportunity to escape taxation on real estate completely if you have reached age fifty-five as of the sale date and have used the property as your principal residence for three out of the five preceding years. This once-in-a-lifetime exclusion is available for gains up to $125,000 so take it when and where it will do the most good. You get no credit if you are unable to use it all;

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it can't be saved. If Mr. Dough, in our previous example, had elected to take the once-in-a-lifetime exclusion on the sale of house A, it would have eliminated the tax on a capital gain of $20,000. If however, he took it on the sale of home B, the exclusion would have saved the tax on a $70,000 gain!

If the property is jointly owned and one party qualifies, both are deemed eligible. If you divorce after being party to such an exclusion with a former spouse and if you jointly buy a home with your new spouse, neither of you will be eligible for the exclusion. If even one party is disqualified then automatically both are. Remember, this exclusion is available even if you choose not to reinvest in another home at all.

GIFTS

Of course if you give property away you eliminate the taxes which might otherwise accrue. There are gift taxes but since ERTA (Economic Recovery Tax Act of 1981) the gift allowance is quite generous. As mentioned earlier, you are allowed to give each year, to separate individuals, $10,000 free of taxation or $20,000 as a couple if your spouse joins in the gift. The donee (person who receives the gift) can be a stranger or a family member. If a family member is a donee the hope would be that that person is in a lower tax bracket than the donor and so,. although the asset would remain within the family, the tax liability would have been reduced. This is commonly referred to as "income splitting". Progressive tax rates encourage citizens to find ways of staying in lower tax brackets. One way of doing this is to divide income between several taxpayers keeping them all in low brackets. If $1,000 is earned by someone in the 50% bracket , $500 goes to the federal government in taxes. If the income is made by someone in the 12% bracket, only $120 goes to the federal government.

ERTA, in 1981, made it possible to gift an unlimited amount for tuition or medical expenses as long as the gift was paid directly to the qualified institution on behalf of the donee.

Minors can receive in their own name life insurance policies on their own life, U.S. Savings bonds and savings accounts. Interest income is taxed directly to the child in his own tax bracket. Provision has been made for minors to receive other property via Section 2503(C) of the Internal Revenue Code, the Unified Gifts to Minors Act or regular trusts. Just which vehicle to use in transferring property should be determined with the advice of you attorney.

Gifts will be discussed in greater detail when we reach the section on estate planning.

SHORT TERM TRUSTS

Short term reversionary rusts, commonly called Clifford Trusts, must continue for at least ten years and a day. The idea behind them is "income splitting", but in this case the donor can get the asset back when the trust expires. Short term reversionary trusts have been widely used as vehicles to fund childrens' education expenses. The tax saving is large when you consider a $40,000 education at a four year private college might cost a fifty percent tax bracket benefactor $80,000 in before-tax dollars. If, however, the $40,000 were transferred to a Clifford Trust the actual cost of educating a youngster would effectively be cut in half. If appreciating assets are

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used to fund the trust any capital gains that might result are taxed to the trustor (benefactor or person who establishes and funds the trust). If income, usually in the form of interest, dividends or rents, is currently distributed (i.e. during the trust's life), the beneficiary pays the income tax, but if income is accumulated, then the trust itself would be liable for the taxes.

UNITRUSTS

Unitrusts, sometimes referred to as charitable remainder trusts, are still another form of gifting and income splitting. They generally work like this: A sets up a trust from which his child B is to be paid at least five percent of the trust's assets on an annual basis for a specified number of years, up to twenty or for life. When the trust terminates the remaining assets go to charity. A, upon establishing the trust, takes a deduction for contribution to charity, the amount being determined by the value of the charity's remainder interest. Additionally, A is allowed a tax lowering deduction and also escapes any capital gains taxes which might otherwise have come due on appreciated property. For instance, if A's tax basis (basis = price originally paid for the asset) was $10,000 and the value of the asset when transferred was $50,000 there would have been an $8,000 capital gains tax, assuming A was in the fifty percent tax bracket and disregarding interest and other refinements. ($40,000 profit taxed at capital gains rates on only 40% equals $16,000 to be taxed in your tax bracket which, if it should be the 50% bracket, equals a tax due of 1/2 or $8,000).

The charitable lead trust is almost the opposite of what we have been discussing because the current income is given to charity and the property itself is kept. In this manner a large amount of income taxes may be eliminated even though a deduction generally is denied.

Various trusts and their use as vehicles to reduce a person's taxable estate will be explored more fully in the estate planning portion of this book.

CROWN LOAN

A Crown Loan is an interest-free demand note, the interest portion the IRS unsuccessfully attempted to tax as a gift. Mr. Crown transferred almost $2,000,000 to his children payable on demand and the IRS argued not only the demand for return of the money might never be made (sham) but the interest foregone on the debt constituted a gift. The tax court ruled on these issues in Mr. Crown's favor making this an alternative to discuss with your attorney. (There are pitfalls that cannot be discussed in a book of this length.)

MUNICIPAL TAX-FREE BONDS

The interest on state and local government bonds is determined by multiplying the coupon rate by the par value. Taxes are not levied on this income to the bond-holder which makes Municipals especially attractive to taxpayers whose income tax-brackets allows them to achieve a larger after-tax net return from tax-free interest than form higher but fully taxable interest. You can see that a tax-free municipal bond returning 10% might be a better buy than a corporate bond yielding 14%. A 50% tax-bracket buyer would get 7% on such a corporate bond but a 28%

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bracket buyer, on the other hand, would obtain a slightly higher yield of 10.08% on the corporate bonds.

Elimination of taxes should never be the main reason you enter an investment; yield, growth potential, safety and your other assets must all be taken into consideration (use Sydl P. Taccfl).

DIVIDENDS AND ALL SAVERS CERTIFICATES

The first $100 ($200 for joint returns) per year of dividend income from common stock is excluded from your income fro tax purposes.

ERTA also made possible a once-in-a-lifetime income tax exclusion of interest on specific qualified savings certificates issued for a limited time (between September 31, 1981 and December 31, 1982) by qualified institutions.

ACCEPTANCE

"There's this to be said about taxes- if the taxpayer is alive, he's kicking!"

If you're one of the rare people who is willing to accept taxes, chances are you pay little or none at the moment.

Several years ago James Stanbery, in speaking of the unfairness of our present tax system, compared the hardship of imposing even the lowest percentage of taxes on low income earners with the total lack of inconvenience that results when high income earners pay their taxes. When he spoke for the Populist movement in California the highest federal income tax rate was 70%. He seemed to bemoan the fact that 70% tax on a million dollar income would leave the taxpayer a hefty and, he seemed to imply unjustifiable $300,000 to live on I wonder how long he thinks our high-bracket taxpayer would be willing to work and risk for the privilege of providing 70% (currently 50%) of the results of his efforts to the federal government?

An old Arabian proverb advises: "Do not cut the tree that provides shade."

If you are among the majority of "kickers" who choose not to accept taxation meekly and with good humor there is something you can do besides postponing, eliminating and reducing your taxes as advised here; that is educate others. President Cleveland is credited with the firm belief that people should support their government but the government should not support the people.

If you choose to accept taxes as they stand you are opting for the illusory governmental safety net which is supposed to protect citizens from the consequences of their own judgments, decisions and actions.

I want to share with you the thought Thomas Jefferson had on the subject of accepting taxes:

> "The suppression of unnecessary offices, of useless establishments and expenses, enabled us to discontinue our internal taxes. These covering our land with

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officers, and opening our doors to their intrusions, had already begun that process of domiciliary vexation which, once entered, is scarcely to be restrained from reaching, successively, every article of property and produce."
--- *Forbes*

REDUCTION

There are more ways to reduce your taxable income than I can hope to mention here, but depreciation is one of the most recognized and widely used methods.

Most things lose their value as they are used over a period of time. Deductions for depreciation are allowed on this theory even though in actuality the value of real property and even some automobiles seems to increase rather than decrease over time. The depreciation rules are varied and tend to be complex. ERTA provided for faster write-offs referred to as ACRs (Accelerated Cost Recovery) than were available before 1981. These predetermined recovery periods are shorter than useful lives and extend to industrial plants, machinery, trucks, automobiles, equipment and other personal as well as real property.

A taxpayer has the option to use straight-line, extended or accelerated recovery periods. There are pros and cons connected with each one depending on an individual's unique and overall financial picture. This is an area where and accountant or tax attorney should be consulted with the objective of analyzing the type of depreciation you should elect in a a given situation.

REAL ESTATE

Real Estate could not really compete as an investment were it not for all the deductions that investors area allowed. Less well known are the deductions available, at least on a temporary basis, to a homeowner.

Suppose your job takes you to another locality for a few years or you are retired and travel extensively, it is possible to rent your residence until you return to it and receive special tax benefits at the same time. Mortgage interest and property taxes are always deductible on a personal residence but additional deductions are available to income property such as utility and insurance payments, maintenance expenses and depreciation. Often these deductions outweigh any rent you may receive. Also a tax loss may be desirable to offset personal income taxes. Remember, though , when it comes to selling a personal residence in the future your tax basis in the home must be reduced by any depreciation expenses claimed while enjoying rental proceeds from the property.

THE "AT RISK" RULE AND "PHANTOM INCOME"

The "at risk" rule was initiated in the tax reform of 1976. Basically, it states you cannot write-off more than the amount you have actually put into an investment unless you are "at risk,": meaning personally liable for the "extra". Real estate is an exception, and that is one more reason it is such a popular investment, but even so one must beware of " phantom income."

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The windfall of being able to take more deductions than the amount you actually have invested in a project is an illusory benefit referred to as "phantom income." Deductions reduce your basis in an investment so if it should be a losing proposition you are taxed to the extent that the sales price exceeds your basis. The "extra" deductions above your actual investment will be taxed as ordinary income.

DEDUCTIBLE CONTRIBUTIONS TO RETIREMENT PLANS

We have previously discussed IRAs, KEOGHs and other pension plans in some detail and realize that thanks to ERTA, contributions by an employee to his own plan are deductible and, of course, the interest, dividends or other profits that accrue within the plans are tax-deferred.

You must start withdrawal of retirement benefits by age 70 1/2. Any money left in the plan after age 70 1/2 must be withdrawn at least as fast as a schedule that would reduce the balance to zero over your expected life span as determined by actuarial tables.

Altogether, with a KEOGH of $15,000 and a maximum IRA contribution for a couple with a non-working spouse of $2,250 it is it is possible in 1983 to deduct $17,250 annually and even more after 1984. If you are qualified for the KEOGH by only part-time self-employment you might be able to deduct even more if you also contribute as an employee under a company plan. It is not a good idea to fund your IRA with tax-advantaged investments such as municipal bonds unless you expect to be in a high bracket after retirement!

GOOD AND BAD TAX SHELTERS

The IRS Code provides for legitimate shelters as an incentive to investment.

Abusive tax shelters often have inflated appraisals, unrealistic allocations and involve improper, extreme and even illegal interpretation of the law. Often incomplete or misleading facts are presented in order to obtain substantial tax benefits. These are in reality frauds. They are frequently characterized by forged trading records, phony transactions, false affidavits, illusory notes and postdated documents.

Roscoe Egger, commissioner of Internal Revenue, favors the "out-of-pocket" approach which allows a deduction to the extent of the cash investment in the initial year of an investment. Under this approach taxpayers will receive a dollar deduction for each actual dollar invested and no more!

HOME OFFICE DEDUCTIONS

Since 1981 the rules qualifying deductions for home offices have become more lenient. The test for such a deduction is that the "office" be used exclusively and continuously for purposes of trade or business and unless you are self-employed the home office must be for your employer's convenience rather than your own.

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If you qualify you can deduct part of the expenses you incur in running a home,; mortgage and insurance payments or rent, utilities, taxes and maintenance in proportion to the ratio your "office" bears to the entire dwelling. Even certain pieces of furniture and business equipment may be depreciated and written off over time in a prescribed manner.

A recent court ruling even allowed deductions for part of a room because the exclusive business use could be shown even though there was no tangible separation form the rest of the house. However, a partition or some sort of divider as well as removal of an and all personal non-business related furniture would be advisable if you think you might find such a deduction worthwhile and justifiable.

CREDITS

Credits are the best thing that can happen to your tax bill! See page 224. Remember they don't just reduce your taxable income they reduce your tax bill directly. Various credits can be taken for rehabilitating real property under qualifying conditions as to age and use, for child-care, for installing insulation, weather-stripping, solar collectors, wind-driven generators for certain hiring practices, political contributions and in some instances simply for being a senior citizen, or as Helen Hayes would say, a "grandperson"!!

NOT SUCH GOOD NEWS

Not all of the recent tax reforms have been met with cheers. You can only deduct medical expenses that exceed 5% of your adjusted gross income. Also since 1983 you can no longer deduct half of your medical insurance premiums but now these premiums will be treated as just another medical expense.

As I write this there is an effort afoot to limit deductions for interest payments, except those on residential mortgages. Also to limit the tax deduction on employer contributions to employee health plans.

The alternative Minimum Tax was enacted to make certain members of the most affluent segment of our society do not manage to escape without paying any taxes at all. A 1971 news headline informed us that 276 people with incomes over $100,000 each paid no taxes whatsoever in that year. The Alternative Minimum Tax is computed by adding any tax preference items (such as accelerated depreciation, the excluded 60% portion of capital gains, excluded in interest, costs and certain expenses connected with mining, oil drilling, etc., etc., which do not concern the average middle income taxpayer) to adjusted gross income and then subtracting, certain itemized deduction and specified exemptions which will yield the Alternative Minimum Tax base. This is taxed at 20% and must be paid if it is higher than an individual's tax computed in the regular manner.

Today there are approximately 300,000 shelter returns under examination by the IRS and 16,000 pending before the tax court. This constitutes 30% of the total docket (load). Many errors the IRS catches are its own. One study showed 63% were made by IRS data processing personnel as

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opposed to 37% by taxpayers. Thanks to the new tax law TEFRA (Tax Equity and Fiscal Responsibility Act) the IRS needs to revise fifty-one forms and thirty-eight publications.

SUMMARY

In general, if your goal is to eliminate taxes the only way it can be achieved is by losing or giving your money away, with the one exception discussed involving your personal residence once you have reached age 55. If you make money on your investments taxes must be paid eventually; the trick is in the timing! Remember this section is called Tax Management not Tax Evasion.

Anytime you can postpone income tax liability it is to your advantage to do so. You can take the money currently and invest it so that it will have multiplied by the time the tax has to be paid. Just as you might employ a hired hand on a ranch even though he is supposed to report somewhere else in a few months, you could continue to have that money work for you even though you know it is eventually earmarked for taxes and the IRS. Uncle Sam may get it sooner or later but you can keep the fruits of its labor!

Anytime you are able to shift earned income to another taxpaying entity which is in a lower marginal income tax bracket, overall tax savings will be achieved. Sometimes the shift is accomplished by setting up trusts. One of the benefits of incorporation is the fact that a corporation is a distinct entity which is taxed at a lower rate than is an individual earning the same income. Also shifting the income itself which would normally be taxed at ordinary tax rates to some form of tax advantaged income such as real estate with its depreciation, deductions and capital gains treatment will all help to make you a winner!

Worksheet - Chapter Twenty

Always ask concerning a potential investment:<

1. Is it a "good" investment on its own merits?

2. What is the tax impact to your overall financial situation?

3. Is this a "preference" item?

4. Have you checked to see how you stand with the minimum tax regulations?

5. Is it liquid?

6. When liquidated how will it be taxed?

7. Considering your current and anticipated tax bracket, how advantageous is tax exempt income vs. taxable income?

8. Can you sell any "losers" in your portfolio to offset current gains?

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9. Are you taking advantage of the lower long-term capital gains taxed wherever possible?

10. Have you considered giving appreciated long-term capital gain assets to charity?

11. Are you taking depreciation where allowed? Credits?

12. Have you considered ways to delay taking current income?

13. Have you been using exchanges to defer taxes?

14. Have you taken the provision for "stepped up basis" into account in your planning?

15. When selling stock acquired over a long period of time do you consider which certificates are best to sell for tax advantages?

16. Are you currently or have you considered the advantages to be gained form using trusts in your planning?

17. Are you taking advantage of IRAs, KEOGHs and other estate building plans?

18. Are you earning the highest possible after-tax total return on your present investments?

19. Have you considered the merits of 10-year-averaging available for lump-sum distributions?

20. Does a lifetime giving program make sense to you considering the $10,000/year you can give free of gift taxes to an individual?

Compare the before and after tax yields of the following:
(those you own or would consider investing in)

- bank savings certificates or certificates of deposit
- money market funds
- corporate bonds
- "deep-discount" bonds
- corporate bond funds
- convertible bonds
- municipal bonds
- municipal bond funds
- writing options
- common stock
- preferred stocks
- convertible preferred
- mutual funds
- buying new issues
- U.S. Govt. Securities
- treasury bills
- treasury notes
- treasury bonds
- Ginnie Mae pass-throughs
- investment real estate
- variable annuities
- buying puts and calls
- trading in commodity futures
- oil/gas leases
- equipment leases
- selling stock short
- precious metals
- diamonds & other gems
- collectibles

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Recommended Reading
Chapter Twenty

Everything written by B. Ray Anderson
Business Use of Your Home, IRS publication 587
Beat the IRS Legally, by Andrew Ciaramitaro
The New Tax Law and You, by Jerome Tuccille
How You Can Get the Most from the New Tax Law, by Smith and Spragens
Perfectly Legal, by Steiner and Kennedy
Everything You Always Wanted to Know About Taxes, by Michael Savage
Real Estate Taxation, by Jeddeloh and Perkins
Real Estate Tax Shelter, by John C.M. Wilkinson

Chapter 21
"Sounding Off"

Taxes are as old as recorded history. They are mentioned in ancient Sumer around 3,000 B.C. Tithing, the practice of pledging 10% of one's wealth, was commonly practice among ancient peoples and still is used today by some religious groups in the United States.

Rome collapsed when taxation reached 52% and when taxes imposed on the colonies reached 23%, that was considered excessive enough to start a revolution with Britain.

It is interesting that prior to 1862, the federal government was supported by revenue from import duties and proceeds from the sale of public lands. It was only in 1862 that the Bureau of Internal Revenue, income and other internal revenue taxes were all established in order to finance the Union in its war against the South. After the Civil War IRS activities declined dramatically only to emerge again in full force after the passage of the Sixteenth Amendment in 1913. The Sixteenth Amendment, authorizing our present income tax, effectively canceled Article I Section 9 Paragraph 4 of our original constitution. The drafters of that original Article knew full well what they were doing when they expressly forbade taxation on an individual's income. "The power to tax is the power to destroy." is a quotation that rings true!

PROGRESSIVE OR GRADUATED TAX

The progressive tax embodies the idea that people with higher incomes should bear relatively more of the country's tax burden. In fact, I recall reading, but I'm not sure where, that it is a "long-standing principle" that a person should be taxed on his ability to pay. Apparently the writer believed this statement fell into the category of facts beyond dispute such as "babies should be loved" and "redwoods saved". Upon reading the statement I remember thinking it had been around about as long as Marx and Lenin. Perhaps a less disputable fact in America might be the concept of private property and freedom. Being required to give half of the fruits of your labor to government so that it in turn might distribute it to others less productive, energetic, willing to take risks, lucky, fortunate or less anything, is an effective means of "communizing " a society.

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Politicians are frequently quoted as bemoaning the fact that any reduction in taxes will "cost the government", "the government will lose." The implication is of course, that the government owns or at least has a right to everything a citizen has. The concept that you are government property allows the government to tax as it does. The IRS graciously allows certain deductions as we have seen, but only if you can prove they are justified. The principle being not that the money is yours and may we have some please, but rather that your earnings belong to the government and the burden is on you to prove you are entitled to keep any!

A LITTLE HISTORY

Where and when did this thinking originate?

In 1928 government at all levels spent less than 10% of the gross national product. Two-thirds was spent at the state and local level which meant that less than 3% of the national income was spent by the federal government in 1928. Almost fifty years later, in 1977, total government spending had risen to 40% of the gross national product and two-thirds was federal spending! Out of every dollar a citizen spent in 1977 the federal government controlled $.40 of it.

Million Friedman, the notable prize winning economist, has pointed to the 19th century as being one of the most productive periods in history, not just for the robber barons, but productive for the common man. Illiterate immigrants were received into this country in droves and progressed at a rate that would make a person's head spin today. They were able to improve their condition and that of the nation because they were limited only by their own imagination and endurance; the United States was indeed a free society. Of course, there was poverty and misery but it was more easily endured because it went hand in hand with hope and opportunity. Even if an immigrant working on the railroad or in the sweatshops realized he might not obtain the riches of a robber baron, he felt one day his children might. The dream was fresh, sweet and motivating. During this time in her history, America cam closer than ever before or after to embracing the free enterprise system.

Forbes Magazine, in its "Thoughts on the Business of Life," quoted Herbert Hoover:

> "It has been dinned into us that this is the Century of the Common Man. The idea seems to be that the Common Man has come into his own at last. But I have never been able to find out who this is. In fact, most Americans will get mad and fight if you try calling them common I have never met a father and mother who did not want their children to grow up to be uncommon men and women. May it always be so. For the future of America rests not in mediocrity, but in the constant renewal of leadership in every phase of our national life."

FREE ENTERPRISE VS. SOCIALISM

Free enterprise implies freedom to establish an enterprise. It is the antithesis to the myriad of fees and regulations and certifications a person has to go through today to engage in business.

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Some people support socialism, figuring that if widgets are going to be manufacturer or gidgets produced why shouldn't the government reap the benefits (profits) rather than a private entrepreneur? The answer: The entrepreneur has to satisfy his customers and the government doesn't, a fact which Soviet citizens can verify. Quality is one of the main difference between forced an voluntary exchange; the other is efficiency. In 1982 it was reported that federal workers had salaries 35 1/2% higher than workers in the private sector. It is estimated that anywhere from 150,000 to 400,000 federal jobs could be taken over by private enterprise. However, the vote of federal employees is important to every politician and certainly none want to be blamed for taking away federal employee jobs!

On the other hand, there have been abuses in our system, in our Government's honest attempt to provide for the" general welfare " Article I Sec. 8 U.S. Constitution) which have resulted in the ridiculous situation where not working, while not being as lucrative as having a federal job, has been more profitable than working in the private sector.

It is certainly no incentive to work when it's possible to get the same income form transfer payments that a worker who pays taxes must earn. There have been cases where a wage earner has been penalized because of working, paying taxes on his earnings rather than sitting back and receiving the identical amount through government auspices tax free!!

If transfer payment such as unemployment compensation, pensions and disability payments for instance, were taxed, the truly poor wouldn't be touched because they would remain below the cut off point which requires taxation anyway. As we saw in chapter nineteen, unemployment compensation is taxed if your total income exceeds $20,000 so this is not a new or radical suggestion. Many of the people getting "transfers" already have adequate assets and although they naturally would resent paying taxes on this additional income, for which they qualify, there is no rationale for them to avoid paying taxes, or in some cases even accepting it (social security, for instance.)

For example, a retired lady recently consulted an investment adviser in our area because she had $200,000 in a money market fund coming due and didn't want to put it any place that would give her interest because that would raise her income and make her responsible for more taxes. She didn't need more income because she was already living comfortably on her husband's pension and social security.

About half of all government transfers come in the form of social security pension payments. Because the capital has not been properly invested, as in a qualified pension plan, to refer to social security as a pension at all is a farce, but one which the government perpetuates. It would at least show some consistency to exempt the contributions and tax the benefits as in a private pension plan.

The progressive tax punishes human effort! High bracket tax payers do strange and often non-productive things (like digging dry holes) in an effort to reduce their tax bite. Although attorneys and accountants and fast talking promoters may benefit, the government ends up collecting fewer dollars and society suffers because of the misallocation of capital. Our gross national product is less, thanks to tax distortions. many Americans feel pressured to make their investment decisions

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on the basis of complex tax calculations rather than on the economic merits of the particular situation. We are faced with the ludicrous situation where our tax law dictates how our economy operates!

CORPORATIONS

Legislated and pointed tax reductions unintentionally shift capital within the corporate sector by providing tax breaks for investments that would otherwise be insufficiently profitable to attract investors. This is a way of subsidizing inefficiency. Even worse is the fact that unwarranted expansion and conglomeration are the natural results of corporate retention of earnings. With so much capital staying within the organization instead of being returned to the investors as taxable dividends, corporations start to behave like investment trusts; themselves buying investments and planning mergers. Additionally, the government fails to receive revenue from the dividends that aren't issued and instead has to be content with receiving half the tax revenue at a later date in the form of an individual's capital gains. Since interest payments are deductible, corporations are encouraged to borrow to obtain capital as opposed to selling stock on which nondeductible dividends must be paid. Since it is easier under our present tax system, to shelter investment income from high tax rates than it is to shelter salary income, we get the phenomena of people with the highest income actually paying less taxes than many middle class salaried workers. It is really the people who consider themselves egalitarians who should be behind the idea of repealing the corporate tax because it has been shown that the wealthy pay less tax under existing law than they would if corporate taxes were integrated into the personal tax.

CORPORATE TAXES

On January 26, 12983, Ronald Regain was quoted in Boston as saying he wished to abolish the corporate income tax. The media immediately made him a laughing stock. After all, over $58 billion dollars is annually pumped into the treasury making up 9% of all federal tax receipts. The president pointed out the not-so-earthshaking fact that corporations are owned by people who would continue to pay the tax as individual investors at rates that might well be less than the maximum corporate tax rate and would therefore achieve savings.

Tax-exempt institutions pay corporate taxes indirectly through their investments in profit making businesses and would also benefit if taxes were not first paid by the corporation as a distinct entity. I have the following quotation in large letters on my office wall: When are we all going to have the courage to point out that in our tax structure the corporate tax is very hard to justify?

Where is the justice in first levying a 46% tax on corporate profits and then on top of that, taxing individual dividends? This is a blatant example of double taxation and Americans are just taking it on the chin. Most politicians try and make you forget that corporations are made up of millions of small shareholders. There's a good chance you are one of them, if not directly then indirectly through your mutual or insurance fund, labor union pension funds or other retirement accounts or relationship with a large tax-free institution (deduction, medical or religious) whose endowment may look like it is invested tax-free but who in reality is paying the 46% corporate tax before they ever get hold of their supposedly tax-free dividends.

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President Reagan didn't expect the government to give up revenue by abolishing the corporate tax, he thought instead there would be a net gain all the way around.

A.F. Ehrbar, in an article he wrote for *Fortune* Magazine some years ago, pointed out the merits of abolishing corporate taxes. If corporations were taxed like partnerships, each shareholder bearing his share of the tax burden on a pro-rated share of the earnings, the corporation as a separate entity would be free from taxation and society as a whole would benefit. Part of the present corporate tax burden is passed on to consumers and acts like an "erratic sales tax that falls unevenly on different goods and distorts the output mix." Shareholders respond to their share of the present double taxation by investing in non-corporate areas with lower value to society but better after-tax consequences to individuals. This is a prime example of the distortions our present tax system causes.

Former Secretary William Simon championed the merits of abolishing the corporate tax way back in 1975 and even Jimmy Carter jumped on the bandwagon for a while. Ehrbar suggests that really corporate profits should be ignored because reported earnings aren't actually income and tax should fall only on the dividends and capital gains of individual shareholders. He adds, however, that such an idea is a political impossibility because "the loophole baiters would never be able to resist screaming about all those reported profits that were not being taxed at all."

The following is a quotation from the Wall Street Journal's report of President Reagan's infamous "Boston Remarks" the end of January 1983 as reported by Rich Jaroslavsky:

> "White House officials, reacting to the potential for political damage, scrambled to play down the significance of the president's comments."

When I was in grammar school Harry Truman was President and I remember no one particularly liking him everyone criticizing and yet admiring him at the same time. I remember hearing over and over, "well, by G-d, he has guts!" Because he stood behind his beliefs, the country seemed to stand behind him. I don't know if the could or would have been allowed to take stands today with public relations men and pollsters weighing the effect of every word and trying to "clean it up" for public consumption so that no one is offended. Putting a politician in the best light is not necessarily putting him in a true light.

CAPITAL GAINS

Ronald Reagan would like to lower capital gains tax rates because he said history shows with each reduction in the rate the government has actually increase its revenues because capital gains investment and sales become so much more attractive.

The proposal to halve the long-term capital gains period to six months from its present one year holding period was attempted in both 1981 and 1982. The rationale behind the move is that capital is presently locked into assets longer than would be justified on a pure investment basis. There have been many changes in the capital gains holding period over the years. From 1922 to 1933 the holding period was two years. In the three year period from 1934 to 1937 it was changed four times ranging from one to ten years! From 1938 to 1941 there were two periods;

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eighteen months and two years. The six month holding period was the norm for thirty-six years between 1942 and 1976 when the tax Reform Act lengthened the holding period in stage beginning in 1977 to nine months to one year in 1978 where it has remained in spite of efforts to shorten it again. in 1978 there was a significant cut in the capital gains tax from 49% to 28% and in 1981 down to the present 20%. When the capital gains tax was reduced, tax revenues on capital gains increased as supporters of the reduction had promised.

INDEXING--COST OF LIVING ADJUSTMENTS

Over two centuries ago indexing was referred to as tabular standard. The idea dates back at least to 1707 when it was developed in response to ethical and moral needs. If the purchasing power of a person due to receive money in the future were eroded because of higher prices over time (inflation) the unwary would be cheated.

In our recent past U.S. Savings Bonds have betrayed a trusting public. The purchasing power at maturity was less than when the bond was bought at a discount years earlier. That's because the cost of living doubled between 1972 and 1980

Indexing became law in 1981 and is to go into effect in October 1985. Indexing adjusts tax brackets to offset inflation. Without indexing, even though purchasing power remains the same, higher nominal incomes move citizens into higher tax brackets. If indexing takes place the government will be denied a revenue windfall. Taxes have not had to be raised (always unpopular with the voters) by the legislators because inflation automatically raised them by carrying the taxpayer into higher and higher brackets. The taxpayers' tax burdens increased at a faster clip than did their income

The funny thing about indexing is that it helps the low and middle income taxpayer and does nothing for those already in the highest brackets who no longer have to be concerned about "bracket creep". Without indexing the average guy will suffer, not the wealthy!! Without indexing the government is able to raise the taxes of the lower income taxpayers without legislation of any sort but those in the highest tax brackets can be raised no higher and are therefore exempt. How then can those groups that continually cry out for compassion for the poor be against indexing? It makes no sense! The Constitution gave Congress the power to tax but that power has been delegated to inflation and must be taken back by indexing.

C. Northcote Parkinson in his book, *The Law and the Profits*, formulated a law which states: "Expenditure rises to meet the income." In a speech before the Commonwealth Club in San Francisco, California, in the spring of 1983, Milton Friedman expanded the law as it applies to the federal government to read: "Expenditure rises to exceed the income."

Rather than cut expenditures, certain legislators are demanding 265 billion in new revenues through 1988. One party has come up with a proposal to raise revenue by repealing the third stage of the Reagan tax cut and repealing indexing which by itself will raise $90 billion dollars even assuming less than a 5% inflation rate. The third year tax cut amounts to 40% of the entire tax relief package on an income of $25,000 but only 5% on an income of $200,000. again, who will be hurt the most by such actions?

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The argument for killing indexing is quite simple: the government needs the money.

It is a dangerous assumption and one natural to a socialist government not a democratic republic such as ours, that as taxes continue to increase ever higher and higher, citizens will continue happily working as hard and productively as ever turning over a larger and larger share of their income to government. The idea that an economic slowdown could result form an increasing tax burden is one the politicians who are against indexing refuse to entertain.

The facts: When taxes dropped from a high of 70% to 50% for top income brackets, the revenue increased from 77 billion to 85 billion dollars. This only proves the point that the lower the price the more you sell of anything -- even taxes!! Indexing would not be needed if there were no inflation: indexing removes most incentive for government to inflate but, of course, it erodes debt. Government and other borrowers can pay off debt with cheaper dollars. Inflation dilutes the currency. With indexing in place Congress can no longer rely on inflation to do its duty work.

TAX REFORM

In the middle of January 1983, President Reagan made it clear he wanted to overhaul the nation's complicated tax system in order to make it easier for people o understand. This has been a goal of every president in memory. It seems to many that only the wealthy can afford the lawyers and accountants needed to figure out the current complex tax code and this in itself is a strong bias against the middle and lower income taxpayer. The average citizen is no longer able to effectively handle his own affairs but the high bracket taxpayer has an edge. He can enlist professional advice to help him beat the system.

FAIR AND SIMPLE

The goal of tax reform is to achieve fairness and simplicity. The first hurdle to scale is the philosophical differences between those that believe this can be achieved by a flat-rate tax or the progressive system of taxation we have now.

FLAT RATE

There are many variations of flat-rate tax plans but the simplest and least likely to be enacted, is the plan that allows no deductions or exemptions and imposes a 10% to 15% tax on everybody period!

Another plan reduced the number of deductions allowed but includes deductions for home mortgage interest, charitable contributions and medical and health cost. It also provided for a base exemption for the extremely poor and provides exemptions for dependents.

The Bradley-Gephardt plan may be part of the Democratic platform in 1984. It provides for deductions for mortgage interest, social security income and veterans benefits, state and local axes and charitable contributions. It is a graduated tax although it is called a flat-rate tax. Under its dictates, about 75% of the population would pay 14% graduated up for the last 25% of the population to a maximum rate of 28%. It is suggested that because there would be no loopholes

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and therefore better compliance could be anticipated, there would actually be an increase in revenue. By eliminating capital gains and other favorable tax treatment of unearned income the wealthy are supposed to end up paying more than under our present system.

CONSUMPTION OR EXPENDITURE TAX

A consumption tax, sometimes called a progressive expenditure tax, is like our present income tax except anything saved or invested would be deducted from income before actual tax due was computed. If anything was withdrawn from savings and consumed, that amount would be added to the taxable income for that year. Income form capital gains not reinvested would come under the same rule. Any amounts borrowed could be added to income in the year borrowed and deducted from income in the year or years repaid. Even simpler would be the alternative of ignoring the debt altogether-- no more adding in one year and subtracting in another. The simplest solutions are often the best!

One large advantage is that the expenditure tax stimulates savings and eliminates the complexities currently surrounding capital gains and depreciation. The expenditure tax would be expected to raise United States national income 3% or more each year. In a study entitled, Blueprints for Basic Tax Reform" William Simon suggested less paper work would be involved in an expenditure tax than under our current tax system. The opposition comes form those who claim the upper bracket people would do most of the saving and investing thereby deducting those amounts from their taxes and transferring a heavier burden to the less affluent. People with substantial assets are now able to let unrealized capital gains accrue untaxed while wages and savings account interest are immediately taxed. Actually, under an expenditure tax, the middle class would be brought more in line with the wealthy because the tax is based on the amount a person takes out of the economy while an income tax is concerned with how much he contributes. The high living portions of society would end up paying far more revenue and the middle class would get a break so that they could increase their savings. Actually our present system does in fact incorporate some of the features of such a tax with its tax-free pensions, IRAs and taxation of capital gains only when realized, etc.

GOALS

Americans, collectively as well as individually must have goals. What is socially acceptable needs to be reevaluated. As a nation we are responding not going forward purposefully as are other nations, notably the Japanese and Soviets who have well-defined ideologies which have made the people willing to accept sacrifices in order to attain these national goals.

Politicians are always followers not leaders of opinion. Perhaps the closest we have come to formulating national goals was way back in the 18th century when our ancestors ratified the U.S. Constitution. Having discounted our legislators because of their dependence on pressure groups to make up their minds for them, it seems clear the courts then are the sculptors of our national goals. Societies from earliest time have encountered the same problems only in varying degrees and on different scales. Eskimos and certain American Indians are supposed to have dealt with the problem of advanced age by abandoning the elderly whereas the Oriental cultures honored, protected, served and revered those of advanced age and all ancestors. Human sacrifice,

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infanticide, cannibalism, polygamy, euthanasia, torture, all have been socially acceptable to groups of human beings at one time or another. Crusaders in the middle ages wreaked untold carnage in the name of universal truth to which the unenlightened were sacrifices. It is time to face the fact that it is man although he may be divinely inspired, who decided what values a society will embrace and often on rational and popular grounds. A case in point is home ownership; is it as desirable in the 1980s as it was in the 1940s or 50s? Should it be encouraged today and at what sacrifice? Is it a good in itself or would society do better to influence our younger generation towards condominiums and smaller more temporary shelter? Perhaps conservation of resources, safety, encouragement of docility of other notions are more worthy of attainment. tax legislation allows society to express its values by encouraging saving or investments in certain "desirable" areas. Funding abortions or exempting charitable or religious institutions is controversial because taxes collected form evrybody are used to enhance the beliefs of some as against the beliefs of others. In fact, the incredible complexity of our tax system today has evolved as a response to support these special interests. Such complexity may no longer be socially acceptable.

When it comes to taxes, many groups similarly appeal to what they claim are indisputable truths; that the old, the young, the in between; are all entitled to this and this and this! By what authority-- surely not because we are human, so it must be because we are Americans and our courts over time have interpreted" the pursuit of happiness" as meaning the assurance thereof; the 'general welfare" as encompassing everything for everybody just as there is conceivably nothing that is outside interstate commerce as the courts' interpretation of the commerce clause in our Constitution evolved over 200 years.

Up until Franklin Delano Roosevelt's second administration there was almost universal agreement that government's role in the lives of its citizens should be kept to a minimum. Adam Smith whose book, Wealth of Nations, had a profound effect on the framers of our Constitution, saw the ideal society as a place where voluntary cooperation among individuals flourishes and in which each person is free to use his own abilities and resources as he chooses in accordance with his own beliefs so long as he does not interfere with the right of others to do likewise.

Milton Friedman has argued that the greatest danger to free enterprise lies with the intellectuals who are in favor of freedom for themselves and against it for everyone else and the business corporations who think everybody else should be free (independent) but are against it for themselves. Freedom for them would entail giving up tariffs, subsidies and special provisions in the tax code.

The popular columnist, Ellen Goodman, in one of her pieces recently expressed the view that everything is up to "Big Brother," She discussed the "patience" of the unemployed which was about to run out waiting for the Reagan Administration to rescue them.

President Kennedy, when faced with what was in those days a whopping budget deficit of 4 billion and a 6 1/2 % unemployment rate, convinced a defiant Congress that a balanced budget could not be achieved by raising taxes. He discussed his fear that the big spenders would soon be off on another round and we'd end up with deficits all over ad infinitum, Kennedy instead cut income and corporate taxes and increased defense spending at the same time. It's strange that our

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current president, who is often referred to as hard-nosed, stubborn and conservative, seems to emulate both John Kennedy and Franklin Roosevelt whom the media have depicted as two of our most compassionate and liberal presidents. In fact, it is surprising how much like our current Republican President Franklin Roosevelt sounded in a speech he gave on October 19, 1932:

> "If the nation is living within its income its credit is good, If in some crisis it "lives beyond its income for a year or two it can usually borrow temporarily on reasonable terms. but if, like the spendthrift, it throws discretion to the winds, is willing to make no sacrifice at all in spending, extends its taxing up to the limit of the people's power to pay, and continues to pile up deficits, it is on the road to bankruptcy."

A deficit can be financed only by printing dollars which imposes the hidden tax of inflation (remember our earlier discussion of inflation; more dollars chasing the same amount of goods = inflation) or borrowing which removes needed funds from the private to the public sector, plus, of course, the additional cost of interest.

No election has ever been lost on the basis of inflation, but Hoover lost in 1932 and Nixon in 1960 on the basis of unemployment. The average citizen understands unemployment only too well and doesn't understand the ravages of inflation.

LIMITING GOVERNMENT SPENDING

An infinite number of worthwhile and desirable proposals are constantly submitted to Congress. With no limitations on the budget, the list of wants continues to expand. Limiting government to spending a set fraction of its income is more important than balancing the budget. The public's appetite in this realm is insatiable and a constitutional amendment is the only way to limit that appetite or be consumed by it.

The founding fathers knew every individual issue should not be decided by a majority vote. For instance, if it were not for the First Amendment's guarantee of free speech, a majority would prevent the Nazis form voicing their opinions, or the Jews or the Baptists or people with red hair or handicapped, et.,; any group that could not muster a majority.

The First Amendment simply states that it is not the government's business to decide who can speak; it its a guaranteed right. Similarly, the idea behind the constitutional amendment to limit government spending is that the budget should not be left to legislators but that an amount of money determined by the people will be provided and within those confines the legislators will have to allocate dollars to the myriads of good programs clamoring for funding. It has been easy for them in the past to play the part of the "good guy" and fund them all, but with whose money?! The people, if they have had enough, must draw the line. If what we've been hearing lately in the media is any indication then a lot of citizens are ready to say along with Howard Beale in *Network*, "I'm mad as hell and I'm not going to take it anymore!

WHO'S TO BLAME

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We always ask who is responsible; Americans have an almost inordinate need to place blame. The answer must be: "The do-gooders." why? Because they used other people's money (taxes), confiscated by force (law), as opposed to seeking voluntary contributors as non-government entities had done in previous years. Some groups would claim, if the cause were worthwhile and aroused the compassion and support of enough people it would have flourished within the private sphere; witness Red Cross, Salvation Army, Goodwill Industries, etc. If that support was not forthcoming from citizens, then perhaps the program shouldn't have been undertaken with government funds. in this regard we already mentioned the foresight of our founding fathers in not making this nation "majority rule" where minority rights would be abridged. A case in point is the recent legislation affecting orphan drugs. Our legislators decided minority diseases should have subsidized research. Since not enough people would directly benefit from the research private companies would not find such research economic and it would not have been undertaken without government intervention in the form of subsidies. The trouble with the "Do-Gooders" is the fact that it is impossible to be as careful with someone else's money as you would be with your own. Carelessness and waste are inevitable and that was acceptable at first because at the beginning there were more people to pay than there were those seeking help. It didn't take long, however, for the "needs" to mingle with the "wants" and as they both grew, more and more interest groups jumped on the bandwagon.

How do you wind down social programs? It is notoriously more difficult to cancel a program or delete a law than to enact a new one. It is easier to keep on a course of more government involvement but if we do we may well find ourselves in a financial crisis with the resultant loss of freedom that would imply. If a halt is called it will be motivated by disillusionment with "Big Brother" and government inefficiency.

The worksheet at the end of this chapter has a list of priorities. you may be surprised to discover just what you value most when it comes right down to it.

In order to recommend a course of action to achieve an objective, we must first know whether that course of action will in fact promote the objective. That the objective itself is desirable can only be determined by weighing the consequences of not winding down our worthwhile social programs. We just cannot afford any longer to indulge mindless rhetoric such as: "A rich country like the United States should be able to " This "rich" nation is 1.5 trillion dollars in debt - the interest alone is 100 billion dollars per year. That's $33,120,000 per day going out in interest! Or to put it another way: every man, woman and child in the United States owes $60,000! We have not even mentioned the unbelievable fact that our government has guaranteed (bank loans, bonds, pension funds, etc.) two or three time our current debt!!! The poorest citizen is in far better shape than the federal government.

As in every chapter in this book, I do not propose solutions for you, I only hope to stimulate you to seek the answers for your own sake. If not you, who will decide these things?

Worksheets - Chapter Twenty-One

1. Number your priorities - 1-40

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_____ nicer home in better neighborhood
_____ better automobile
_____ boat
_____ airplane
_____ swimming pool
_____ extra time and money for travel
_____ private schooling for kids
_____ more income
_____ less taxes
_____ more and better police protection
_____ more and better fire protection
_____ better libraries with longer hours
_____ better public transportation
_____ cheaper public transportation
_____ more consumer protection
_____ no more nations falling to communism
_____ revival of free enterprise
_____ communism to flourish
_____ democracy to flourish
_____ socialism to flourish
_____ better public education for all
_____ America to maintain #1 status as world leader
_____ America to avoid war
_____ clean air
_____ forests and oceans protected
_____ medical research with new breakthroughs
_____ better health care
_____ cheaper health care
_____ no communist domination of America
_____ no socialism in America
_____ more efficient courts
_____ better maintained roads, bridges, dams, etc.
_____ more parks
_____ more social services (child care, senior programs, etc.)
_____ expanded space program
_____ more children
_____ freedom to worship
_____ better prisons
_____ less regulation by government
_____ right to dissent -- picket, criticize, strike

Recommended Reading
Chapter Twenty-One

DIFFERENT POINTS OF VIEW

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You will be stimulated intellectually by reading any books by:

Ludwig von Mises
Friedrich A. Hayek
C. Northcote Parkinson
Milton Friedman
John Galbraith
Robert Heilbroner
William E. Simon
Howard Ruff
Robert Ringer
Harry Browne
Dougals Casey
Andrew Tobias
Ayn Rand
'Adam Smith'

The Richest Man in Babylon, by George Clason
An Introduction to Economic Reasoning, by Robinson-Morton-Calderwood
The Capitalist Reader, edited by Lawrence Stepelevich
How Much More Equality Can We Afford? by Edgar Browning
Who Bears the Tax Burden? by Pechman and Okner
The World of Andrew Carnegie, by Louis Hacker
The Income Tax: Root of All Evil, by Frank Chodorov
Believing in America, by Bud Shuster
The Spirit of Democratic Capitalism, by Michael Novak
The Next 200 Years, by Herman Kahn
The Golden Egg, by Gerald Carson
Revolt of the Haves, by Robert Kuttner
Half Way to Tax Reform, by Ruskay and Osserman
The California 2000 Campaign, by James Stanberry
How to Cope with the Developing Financial Crisis, by Ashby Bladen
The Fleecing of America, by William Proxmire
Minding America's Business, by Magaziner and Reich
Small is Beautiful, by E.F. Schumacher
Economics from the Heart, by Paul Samuelson
Human Option, by Norman Cousins
The Truth About Supply-Side Economics, by Michael Evans
Dangerous Currents, by Lester Thurow
Making America Work Again, by J. Morton Davis
Budgeting for America, by Congressional Quarterly, Inc.

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Chapter 22
Objectives

We have come to one of the most important sections in this book. Not all of you, despite my recommendations, will formulate goals and periodically reexamine your lives, nor will all of you purchase insurance or invest in the stock market or buy real estate but as the saying goes "There's one thing certain in life; death and taxes".

At the beginning of this book I expressed the view that it was unfortunate that people associated estate planning with death because it prevented them from giving estate planning the consideration it demands. People tend to put of thinking about death. However, everything we have discussed in chapter one through twenty-one has relevance for estate planning; in fact estate planning is almost synonymous with financial planning only "more so"! Estate planners usually have expertise in drawing will, forming trusts and have knowledge about the laws providing for the transference of property after death. It is not surprising then that most estate planners are lawyers.

There are many excellent books in the recommended reading section, most of which cover estate planning more thoroughly than I will attempt to do in this section. Estate planning is a subject flexible enough to embrace a variety of opinions and you should certainly read more than one author before you set about following advice. Even though the California State Bar recently came out with a form for a do-it-yourself will, attorneys often warn against a layman executing a will without professional advice (by the way, so does the California Bar except in the simplest situation and when a person would otherwise be totally without a will because he would not seek professional advice). Books authored by attorneys generally include stories about amateurish attempts at transferring assets or reducing taxes with unfortunate results, while the non-attorney authors always seem to have as one of their prime objective, the avoidance of attorney and court fees. Attorneys are aware of pitfalls that are not apparent to the layman planner. It is not surprising then that I wish to stress the importance of professional advice, particularly in the area of estate planning. Laws vary from state to state and change continually. The lawyer who has prepared your will and trust agreement will inform you of these changes as they occur.

"FAT ED THE HOPPING COP"--

THREE KINDS OF ESTATES

Your "probate estate" consists of all the property that is disposed of by your personal representative after your death. That representative will be either the court-appointed administrator if you die intestate or the executor of your choice if you make a will. In this chapter we will discuss some ways of avoiding probate by having property pass according to the dictates of instruments you set in motion during your lifetime such as living trusts with directions that trust property pass to trust beneficiaries upon the trustor's death, or having property pass due to survivorship rights (joint tenancy) or joint bank accounts. With proper planning, many assets would pass directly to beneficiaries or joint owners without ever passing through the probate court. It is not necessarily desirable to completely avoid probate, however. Most people would

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not care to relinquish all their property to others before their death and would want to leave enough assets in their estate to pay funeral and death-related expenses, current debts and taxes.

The main reasons given for avoiding probate are:

1. Probate can be costly. Fees (court, executor, attorney) are generally based on the size of the estate to be administered (percentage).
2. Court records are "public knowledge".
3. Creditors can reach your assets in probate by submitting claims.
4. Heirs may contest a will.
5. Death taxes may shrink the estate.
6. It may take a long time form the date of your death to the distribution of the assets to your heirs.

We are going to examine three types of estate; your probate estate (COP), your gross estate (HOP), and your net estate (FAT ED).

C O P

THE PROBATE ESTATE CONSISTS OF:

C common ownership of property
(example = your interest as a tenant in common)

O outright ownership of property
(ownership in your name only)

P proceeds of life insurance or other death benefits payable to your estate

The probate estate is actually all the property that becomes a concern of your executor or administrator upon your death.

H O P

THE GROSS ESTATE IS YOUR ESTATE FOR TAX PURPOSES:

H half of jointly owned property (with spouse) and all the value of property owned< jointly with right of survivorship with others except to the extent that "others" can show they contributed to the purchase price of the property.

O ownership of life insurance on your own life

P all the property in the probate estate (above)

You can see the gross estate is larger than the probate estate. Before taxes are levied against your estate, certain deductions and credits are allowed. marital deductions may exempt your entire

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estate form taxes if it is valued at $ 600,000 or less in 1987 (see page 292) and if you choose to take up to the full amount of credit allowed. Remember this is not always the best decision so consult your professional advisor in light of the trust discussion on pages 292, 297-299.

F A T E D

THE NET ESTATE IS WHAT ACTUALLY PASSES TO YOUR HEIRS:

F funeral expenses are deducted

A administration expenses are deducted

T taxes are deducted

E everything - all assets-- that form which you are deducting

D debt is deducted before distribution to the heirs.

This should give you a general view of the three kinds of estates. The remainder of this chapter will discuss the main objectives of estate planning.

REDUCING THE COST OF ESTATE ADMINISTRATION

If you die (without a will), a court-appointed administrator, even though usually a close family member, must post a bond, the cost of which will be charged to your estate. You can, however, in your will, waive the posting of a bond by your chosen executor.

The administrator's powers are derived from statutes and rarely include the flexibility needed to deal with the estate in an efficient manner. If stocks are involved and the market takes a downturn the estate is likely to suffer heavy losses before a court order can be obtained authorizing the administrator to sell. In most states the sale of securities or real estate and the settling of claims requires judicial authorization which is costly in terms of both time and money. The administrator is hindered in his management because of restrictions as to percentages and typed of investment. The restrictions are an attempt to protect the estate but too often have the opposite effect.

CHOOSING THE EXECUTOR

Choosing the executor, the person who will carry out your wishes after your death, is of utmost importance. The executor, like the court appointed administrator or any trustee in charge of properly carrying out the terms of a trust, is considered to be a fiduciary. A fiduciary is basically someone acting for another under the highest possible standard of care and with whom he stands in a unique relationship of confidence and trust. The smaller the estate the more important the selection of the proper executor becomes. One with no knowledge of financial matters could end up losing all the estate's assets rather than only shrinking them as could happen in the case of a larger estate. As mentioned earlier, a court appointed administrator is highly restricted in his

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actions precisely to guard against such a happening. However, you have the right to enlarge the duties and responsibilities of your executor. Even though the executor can rely on the advice of a lawyer or investment counselor, paid for by your estate, it is he and no one else who is ultimately responsible for all decisions and their implementation; it is he who must face the wrath of any beneficiary who fears he has suffered as a consequence of the executor's neglect or incompetence. You should be aware of the commitment you are asking of a proposed executor in terms of time and responsibility. Business and investment experience, integrity and compassion together with a genuine concern for the welfare of the beneficiaries of your estate is a hard combination to find in any one person. Often the best solution is provision for co-executor-trustees with both the trust department of a bank and a family member serving jointly. The bank would provide the more professional and objective financial management and the family member would naturally have a better understanding of the needs of the various family members. However, trust departments will normally only serve as executor of rather substantial estates and this may prevent such an option being a viable solution for most of us.

In discussing wills and trust, arguments will be presented for and against flexibility, but it should be apparent from the foregoing discussion that granting your executor (and/or/trustee) the power to do virtually anything that you could do with your property if you were living, is, even though admittedly unrealistic, what you are aiming for in selecting an executor-- an extension of yourself!

DETERMINING HEIRS

There are no set rules in this area other than the intestacy laws which decide who is to get what after you are gone if you abdicate that responsibility by failing to make a will.

Each family situation is unique and although the intestacy laws, which vary from state to state, try to be fair, they cannot possibly take into consideration the fact that one of your children is handicapped and needs more assets and security than the others; that another child has accumulated a very large estate on his own and most of what you could give him would only push him into a higer tax bracket neutralizing the benefit; that your spouse could never live as you would like on the share the courts would award by law. You know your assets and the people to whom you would like to transfer those assets. The first goal of estate planning is to put you in charge; make you master of your own plan!

THE ROLE OF INSURANCE

In section two of this book we discussed insurance as a means of providing an instant estate primarily for young people who have not had sufficient time to build an estate through investments and savings. An adequate life insurance program is still the most common method used to provide dependents with a comfortable income in the event of an insured's untimely death.

Providing financial support is a prime objective of estate planning, especially when several young dependents are involved. It may be less important when children are grown and on their own and certainly if your spouse has already achieved financial independence.

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PROVIDING LIQUIDITY

There are a number of claims and taxes an estate is responsible for upon the estate owner's death. For instance; hospital, medical and funeral expensel, personal debts to individuals, banks or unpaid bills; state and federal taxes and court and attorney fees can all add up to quite a responsibility.

When we speak of liquidity needs of an estate, we refer to the cash required to cover these cost. If adequate planning has not preceeded the estate owner's death, needless losses may occur to the estate due to a forced sale of assets or business interests. If the estate, through careful planning, had sufficient liquidity such sale need never take place and the estate would be distributed to the beneficiaries intact. If some assets had to be sold, planning would allow the executor to take advantage of timing and the best marketing skills in order to obtain the maximum value from those assets.

BUSINESS CONSIDERATIONS

If a portion of your estate consists of business interests such as a proprietorship, partnership or membership in a closely held corporation (a corporation not traded on a recognized stock exchange but held by a close group like a family) there may be a problem of setting a value upon those holdings for estate tax purposes. Since there may be a limited market for such interest, the valuation is reached in a roundabout manner.

First, the underlying worth of the business is determined by looking at earnings, the capacity to pay dividends, the net asset value and market comparisons with similar businesses; then discounts are allowed for a variety of reasons having to do with the non marketability of the asset to the public at large. Naturally the discounts result in al low value for such interests and save estate taxes as well as making lifetime gifts an attractive tool for transferring assets from the estate inexpensively. For these and other reasons your attorney may even advise forming a closely held corporation.

The other reason business interests demand serious consideration when planning for the preservation of an estate's assets concerns the situation where business interests make up the bulk of the estate. As mentioned earlier, if liquidity has not otherwise been provided, business interests may have to be sold to cover taxes and other expenses with resultant large losses for everyone involved. Surviving partners or shareholders may find themselves forced to terminate a profitable business unless plans were made as to the procedure to follow when a partner or owner dies.

One way to ensure that claims can be paid without a forced liquidation of estate property is to borrow the money from a source outside the estate according to a pre-arranged plan. Life insurance proceeds paid on the estate owner's death to a beneficiary outside the estate who agrees to make the money available for the estate's use is an example. This party may be a life insurance trust set up just for this purpose or an heir who would not want to witness any shrinkage of estate assets and therefore agrees to loan the money. A provision authorizing the trustee to make loans

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to the trustor's estate can be inserted in a funded living trust. Also buy-sell agreements, discussed in the next chapter, are frequently used to provide liquidity via life insurance proceeds

Under certain conditions, section 303 of the Internal Revenue Code permits a corporation to reddem enough stock from a deceased shareholder's estate to pay death taxes, funeral expenses and other costs associated with the administration of the deceased's estate without creating a taxable dividend to the estate or heirs. A condition for qualifying under section 303 is that the value of the deceased shareholder's stock in the corporation comprised at least 35% of his entire adjusted gross estate (FAT ED).

For example: If the estate were valued at $1,000,000 and the expenses demanding liquid assets totaled $100,000 then the gross adjusted estate would be $900,000. If more than $315,000 (35%) of the estate were stock in a closed corporation then the liquid asset could be obtained by selling stock back to the corporation without its being counted as a taxable dividend.

TRANSFER OR DISTRIBUTION OF PROPERTY

Creation of an estate is only half the battle; providing for its conservation is the other half. Deciding on the best methods of transferring what you have so painstakingly built up is the subject of chapter twenty-three. Without a well-designed plan of transfer, your assets may well disintegrate and with them the dreams of your children's future, your business growth and the expansion of that charitable institution you have sought to achieve.

Erosion is most likely to occur at the time assets are transferred. We've already mentioned the corrosive effect of administration costs. Liquidation losses when sales take place at inopportune times in order to meet the cash demands of an estate, and poor management of estate assets. In chapter twenty-three we will discuss what used to be the biggest bite of all - estate taxes- and you will see how recent legislation has made it possible to pass on more of your estate with the least possible tax cost.

SUMMARY

We have looked at some of the objectives of estate planning; providing security and a sense of well-being for the principal, financial support for dependents, reducing costs of administration by reduction of the estate through gifts, providing liquidity primarily with insurance proceeds, maintaining business interests intact; ensuring equitable (not equal) treatment for beneficiaries , and establishing a plan for transferring assets. Some of these, along with additional objectives of estate planning will be considered more fully as you read on.

Worksheet - Chapter Twenty-Two
Estate Planning

1. What portion of your estate will pass outside probate and what amount will pass through probate according to the dictates of your will? Are you happy with the present arrangements?

2. What provisions have been made to enable your estate to meets its liquidity needs?

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3. Are you coordinating the new unified credit allowance with the unlimited marital deduction to avoid "overqualifying" your estate? Do you need help in qualifying the most beneficial amount of property for the marital deduction?

4. Are you making proper use of trusts in your estate planning?

5. Have you coordinated your planning with other family members with potentially large estates? (grown children, own parents, etc.)

6. Have you considered "gifting" property with high potential for appreciation while it is still valued low?

7. Have you planned adequately regarding your business interests?

a) What provisions have been made for the continual operations of your business when you or one of your associates dies, is disabled or retires?

b) Can working capital be kept intact?

c) Is the business readily marketable if it should have to be sold? Has a price been established or means of determining a price agred upon?

d) Will this value affect the liquidity needs of your estate? now?

e) Can ownership in the business be transferred without decreasing the value?
How?

f) Just how can the business continue providing for your heirs in the event of your death?

8. Your planning should be reviewed with an attorney if any of the following take place after a will or trust has been drafted:

a) You move to another state.

b) The birth of a child or grandchild.

c) If there are special circumstances relating to a child such as a disabling handicap.

d) The death of a child or grandchild.

e) The adoption of a child.

f) The marriage or divorce of a child or grandchild.

g) Your own marriage or divorce.

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h) Death of a spouse.

i) Special needs relating to health, education, business or travel.

j) A marked increase in personal wealth such as a substantial inheritance or gift.

k) A marked decrease in personal wealth as evidenced by a business setback or making or a large gift.

l) You join a new profit sharing or pension plan.

m) You purchase additional life insurance policies or annuities.

n) You purchase real property or other equity investments.

Chapter 23
Methods of Estate Transfer

In this chapter we will be examining several methods of estate transfer. At death property is most commonly transferred by the law of intestacy, the dictates of a will or the manner in which title is held. Instructions in testamentary trusts are also used to transfer property after the settlor's death. We'll explore the advantage and disadvantages of making lifetime gifts, providing for buy-sell agreements, creating powers of appointment, establishing living trusts, and deciding how employee death benefits and insurance proceeds should be received.

FORMS OF PROPERTY OWNERSHIP

Property may be owned outright by a single individual who can dispose of it in any manner he chooses (fee simple). Property owned by more than one person may be held as "tenants in common" which means that each person (any number) owns a defined percentage of the entire property. This percentage interest can be treated by the owner in the same manner as he treats the property he holds outright. The property interest may be disposed of by will or, in the absence of a will, according to the laws of intestacy. It may be given away, sold, leased, mortgaged and taken by creditors.

Joint tenancy, with right of survivorship, is another common form of ownership. When a joint tenant dies (and there may be more than two joint tenants in a single property) his interest automatically passes to the surviving joint tenant(s) by operation of laws. The last to survive will find himself the sole owner, free to dispose of the property in any manner he please.

In community property state (Texas, Washington, Idaho, Nevada, New Mexico, California, Arizona, Louisiana and Puerto Rico) most property that is acquired during marriage is considered to be community property in which each party holds and controls and undivided one-half interest. Community property jurisdictions generally recognize separate property also and give the owner spouse complete control over it. Separate property is property which the individual acquired prior to the marriage, inherited during the marriage or purchased with

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individual (not community) funds. So as not to get bogged down on a subject which could easily take up this entire chapter, let me refer you to the recommended reading list at the end of this chapter as will as at the end of chapter thirteen.

The reason it is important to become familiar with the several forms of property ownership or to consult an attorney with the necessary familiarity, is that transfer is automatically effected by some forms of ownership whether you planned it that way or not. Your will is operative on certain types of ownership and not on others. You are entitled to dispose of only your half of anything considered to be community property. You can well imagine the complications that arise when property supposedly held as tenants-in-common or as joint tenants is found to have been purchased with community property funds!

Many times people who are well meaning but have little knowledge of the legal consequences emanating from the way in which title to property is held, attempt to advise you in this area. Beware! This is the domain of a professional versed in the laws peculiar to your state.

GIFTS

Thanks to the Economic Recovery Act of 1981 (ERTA) it is now possible for a donor to give an unlimited amount, tax-free, on behalf of a third party donee directly to an educational institution for tuition or to a health care provider for medical expenses. Additionally, a person is able to give $10,000 annually to as many persons as he would like (or better can afford) $20,000 if his spouse joins in the gift ("splitting"), without incurring tax liability for his generosity.

If a lifetime gift is a capital asset the donee (receiver) takes the donor's basis. if its is a testamentary gift (passing on the donor's death) it would receive a new stepped-up basis equal to its fair market value as of the date the donor died. For example, if A bought stock for $5,000 five years ago and gifts the stock, now worth $9,000 to B, B's basis in the stock is $5,000. If B sells the sock two years later for $10,000 he is then liable for long-term capital gains tax on $5,000 even though the stock only went up $1,000 on the market during the time he owned it. However, if at A's death the same stock was left to B, who two years later sold it for $10,000, B would have to pay a long-term capital gains tax on only $1,000. At A's death the stock acquired a new stepped-up basis equal to its fair market value at the time of A's death, which in the example, we established at $9,000.

ERTA removed a former rule (Internal Revenue Code Sec. 2035(a) which required the transfer within three years of death be included in the gross estate of the donor. However, this requirement still holds true for life insurance policies. Also in order to discourage potential heirs from transferring property in contemplation of the donee's death simply in order to obtain a new-step-up basis upon receipt of the property back from the donee's death, ERTA provides that such property, if given within one year of the donee's death, shall retain as its basis the basis attributed to the decedent immediately prior to death. No immediate step-up in fair market value was allowed.

Still lifetime giving has certain advantages over bequeathing property at death. For one thing, the gift is removed form the donor's estate and thereby escapes estate taxes and administrative

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expenses which are generally based on the value of the estate. If the donee is in a lower tax bracket than the donor, any future appreciation and current income will be taxed at the donee's lower tax rates and the donors can witness the enjoyment and pleasure generated by their largess.

Assuming a person does not exceed his annual gift exclusion limits at any time during his life, that is that he never gives any more than $10,000 ($20,000 "splitting") a year to any one person, then at his death he could leave up to $325,000 free on any federal estate taxes-- that is if he died in 1984. (See table below)

The tax reforms of 1976 replaced the former gift tax lifetime exemption and the estate tax specific exemption with a unified credit. Remember a credit reduces the "tentative tax" dollar for dollar not just the "taxable gross"; a credit is therefore worth much more than an exemption. For example, a $192,800 credit is the equivalent of a $600,000 exemption in 1987. ERTA raised that credit in steps beginning in 1982. A partial table follows:

Year of death or year gifts made	Unified Credit	Exemption Equivalent
1984	$96,300	$325,000
1985	121,800	400,000
1986	155,800	500,000
1987	192,800	600,000

Even if a married person had an estate in excess of $600,000 in 1987, he could pass everything to his spouse tax-free because ERTA provided for an unlimited federal estate and gift tax marital deduction. However, just because you can transfer everything to the surviving spouse's estate without paying federal estate taxes, does not by any reasoning suggest you should do so! Many times taxes will be lower if the estates are taxed more evenly rather than reserving a whopping tax on the estate of the second spouse to die. Overuse of the marital deduction in some instances, could actually result in a wasting of the unified credit. Your professional advisor will help you decide the best way to go. but remember, a great many things must be considered. Full use of the marital deduction should not be made as a matter of course before carefully weighing alternatives.

I have not mentioned the special rules regarding gifts to minors, gifts of future interest, gifts made prior to the creation of the unified credit, etc., so for more information refer to the recommended reading list on page 30 and for advice on your own unique situation, see your tax attorney and/ or accountant. As with all areas in this book, my goal is to whet your appetite for more information and suggest sources for acquiring it. The information should help you understand better the inherent dangers in trying to be a "do-it-yourselfer" in this area and should convince you of the savings professional advice can deliver.

BENEFICIARY ARRANGEMENTS

Death benefits payable under pension plans, deferred compensation agreements, tax-sheltered annuities, profit-sharingplans, IRAs and Keogh plans are another way for an owner to transfer

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what would otherwise have been part of his accumulated estate to a chosen beneficiary and in some instances escape federal taxation. Whether to make the employee's estate the beneficiary of death benefit payments under pension and any of the other employment-related plans was of greater importance before ERTA and the unified credit and unlimited marital deduction discussed above. The fact that there may be considerable income tax savings if one elects to take ten-year-averaging and a lump sum payment must be balance against any possible estate tax savings which might have to be given up in order to take advantage of this benefit.

Certain qualified employee benefit plans, Keoghs, IRAs etc., enjoy all kinds of tax advantages (see "Lump Sum" discussion in chapter seventeen and "Retirement Plans" in chapter twenty), one being that for federal estate tax purposes, distributions to a deceased participant's personal beneficiary are excludable from the participant's gross estate as long as they're not taken in a lump sum. If you want the income tax savings available with ten-year-averaging then benefits can be received in installments over not less than 36 months. However, a lump sum distribution to a personal beneficiary is not subject to estate taxes (we're still talking about the deceased participant's or employee's estate) if the beneficiary irrevocably elects not to take ten-year-averaging and the special capital gains tax treatment that goes along with it.

At any rate, whether savings come from taxation (ten-year-averaging) or estate taxes, assets are passed from the participant in many retirement plans simply by an election to designate a third party beneficiary.

LIFE INSURANCE PROCEEDS

Life insurance often makes up a sizable portion of one's estate. With careful planning, proceeds can pass tax-free outside probate, which means no federal estate tax will be levied nor will the proceeds add to the cost of the estate's administration since none will be required. As we discovered when talking about sources of liquidity for an estate, there may be valid reasons for having the insured own his own policy and having the proceeds paid directly to the estate. Yet another, and frequently better, option is to have proceeds paid to a trust. For now we are only considering the role of life insurance in passing assets from one party to another.

Life insurance proceeds are not taxable when received by a beneficiary unless the beneficiary happens to be the estate of the insured! A person is considered an owner

of a life insurance policy if he enjoys rights that go with ownership such as the ability to appoint or change beneficiaries. Sometimes the insured, owner and beneficiary are one and the same person or two or three separate people. A trap for the unwary lies in the situation where the insured is none person (A), the owner of the policy is a second person, (B), and the beneficiary is till a third party (C).

Let's suppose upon A's death that C receives a check form the insurance company. A's estate is not taxed because A had no ownership rights (referred to as incidence of ownership) and C's benefits, being proceeds of an insurance policy, are not taxed (interest earnings on the proceeds may be taxable, however, if received as income over time) but - and herein lies the trap -- B will be considered to have made a taxable gift to C and will be taxed on the face amount of the policy

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which has become a generally substantial though inadvertent gift. To avoid such a situation it is well to remember that when the insured and the owner of a life insurance policy are two different people, the owner should also be the beneficiary.

BUY-SELL AGREEMENTS

In a business partnership, corporation or other entity with two or more participants, if advance planning is not undertaken and one party dies then that party's heirs succeed to his interest by intestacy or will. This is generally not a desirable situation from the surviving principal's point of view nor is it likely to satisfy the heirs (generally spouse and or children).

Buy-sell agreements are an attempt by the parties to avoid a forced and usually costly dissolution of a business venture due to the death of one of the principals. Such agreements are established by the principals during their lifetimes in order to provide cash to heirs for a deceased participant's interest. The buy-out price is established by a formula agreeable to all the principals and often with provision for subsequent periodic adjustments. The buyers may be individuals or the business entity itself in which case the contract is referred to as a redemption agreement.

Life insurance is usually taken out on each principal in an amount sufficient to cover the agreed upon buy-out price. The value of a deceased participant's business interest is includable in his estate just like any other asset. The advantage of a buy-sell agreement, if it is drawn properly, is that it "freezes" the value of the decedent's interest for estate tax purposes. The Internal Revenue Code provides for the executor of an estate to pay the federal estate tax in installments where a substantial part of the estate consists of closely held and therefore not readily marketable, business interests.

POWERS OF APPOINTMENT

A power of appointment is the right to a person (donee) to decide who shall receive property, how and in what amount. Often the donor wants the decision as to who gets what property postponed until certain events occur or peculiarities of possible appointees can be ascertained. The decision, he feels, would be better made at a later time in another light.

Powers of appointment can be created either as a lifetime gift passed to a donee (also referred to as an attorney-in-fact once he accepts the power) who no longer wants to make such decisions himself or the power can arise by will at a testator's (person who makes the will) death.

If the power is a general power of appointment, the donnee can appoint to anyone including himself as opposed to a special power of appointment which restricts the donee to exercisable the power among a select group specified by the donor. Sometimes the power is execrable only at the donee's death by means of his will (testamentary power) and other times it can be exercised during the donee's lifetime (inter vivos power).

In some states a power of attorney is revoked by the death or incompetency of the donor but in others (including New York and California) there is by statue what is called a durable power of attorney which survives the incompetence of the donor. In fact, in states where durable powers

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are recognize, sometimes they are specifically drawn so that they only spring into effect upon the donor's incompetency. Not surprisingly these are called "springing" powers. Helping to account for their popularity is the fact that when a donor is disabled there is no delay as would normally occur in a court proceeding to appoint a conservator or other legal representative to handle the affairs of an incompetent. However, even a durable power of attorney may sometimes be revoked by a successor in interest to the incompetent donor and the applicable law must be taken into consideration when planning.

The done needn't accept the power; it can be renounced within a specified time, usually nine months, after its discovery. You might ask why someone would want to renounce a power of appointment, especially if it were a general power and he could appoint property to himself or his heirs. Actually, whether he chooses to do so or not the IRS looks at an unexcercised general power precisely as if the donee had appointed the property to himself and should he die not having exercised the general power his estate is increased by the value of "what could have been." Naturally a special power of appointment does not carry the same tax consequences and therefore provides both a useful and flexible tool for estate planning which is frequently used in conjuction with trusts.

TRUSTS

Trusts have been touted as the answer to every and all estate planning problems. That may be an exaggeration but it is hard to imagine an estate where some type of trust could not be used beneficially.

When you (interchangeably referred to as the settlor, trustor or grantor) give property in trust to some person or entity (called the trustee) for the benefit of others referred to as beneficiaries) you are simply trusting someone to handle your property for the good of the third party. The settlor (you) decides the rules under which the trust will function.

There are revocable trusts which means the settlor reserves the right to change his mind and cancel the whole thing right up until the time of his death, and there are irrevocable trusts- once made they are final- they can't be undone (with special exceptions that don't concern us for the purposes of this discussion). Just as with the powers of appointment, there are both inter vivos (living) trusts and testamentary trusts that take effect only at the settlor's death. Trusts may be funded (property transferred into them at the time they are created) or unfunded with property to pass into them on the happening of certain events.

It is generally possible to reduce the costs of administration, avoid publicity and soften taxes by creating a trust during the settlor's lifetime and then have him will all or most of his assets to the trustee to be held subject to the provisions of the trust. Death benefits and life insurance proceeds can be received by such a trust thereby avoiding estate taxes. These trusts are commonly referred to as pourover trusts because assets are poured into them via the terms of the will.

Irrevocable trusts are often created to save taxes. You, as settlor will not be taxed on trust income as long as it is not used to discharge any of your own legal obligations or pay premiums on insurance on you or your spouse's life. Distributed income is taxed to the beneficiaries who

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receive it, and who are hopefully in a lower tax bracket then the settlor, or to the trust as a separate taxpayer is the income is accumulated. When the funds are finally paid out to beneficiaries they receive credit for the taxes already paid by the trust according to a specially computed formula. This is refereed to as the "throw back rule."

However, revocable trusts have no such tax advantages since the settlor has the power over the assets at all time (after all, he can revoke the trust anytime he desires and embrace the assets.) Income from a revocable trust is taxed to the settlor during his life and the principal is taxed to the settlor's estate when he dies.

But there are, of course, a myriad of reasons to create a trust. A settlor may seek relief from managing his estate during his own lifetime and be willing to pay for the professional services of a trustee. He may even feel his heirs are incapable of managing the estate assets after he is gone and he therefore lays out instructions in a trust for their protection and benefit. The fact that trusts by-pass probate may be a very desirable feature, more so to some people than to others. Trusts provide a means of passing property to minors so that a trustee can manage the assets until they are capable of doing so themselves. This bypasses the rigidities connected with legal guardianship.

Revocable trusts may also be used to anticipate the need for management of assets in the event of incompetency. The trustee can often act when the power of attorney is no longer effective. Therefore, a combination of a durable power of attorney and an unfunded revocable living trust may be a desirable plan against incompetency. Upon realization of the donor's disability the attorney-in-fact could simply transfer the donor's asset to the ready and waiting trust thereby funding and activating it. A convertible trust is often used for this same purpose. The settlor of the trust acts as trustee or co-trustee until such time, if ever, that he is disabled whereupon the trust converts to an irrevocable trust for the settlor's benefit and the co-trustee takes over the management.

Trusts allow you to avoid having court administration of your estate (probate) which may be costly, time consuming and embarrassing (public record). You can protect your beneficiaries own experience by providing professional management with the proper trustee or by laying out instructions yourself for their protection and benefit. If the trust is activated during your lifetime, you can preview the management of your after-death estate and see if the trustee is really as capable as you had hoped. This is tantamount to getting a second chance to resolve observable weaknesses and oversights and perhaps substitute trustee. Also, aside from estate planning per se, trusts can be excellent income stretchers as we observed briefly in chapter twenty. You can provide funds for the children's education or support of dependent parents by setting up trusts that will be taxed in brackets lower than yours. In reality, this is a means of expanding your after-tax dollars.

Each state has its own laws governing such things as trustee powers and the length of time property can be held in trust. You can choose the state law you wan to govern your particular trust as long as some material connection with the state of your choice can be observed. It may be that some of the trust real estate is located in that state or that it is the principal place of residence of the settlor or the trustee.

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Your attorney is your best source of information, regarding trusts. However, to reiterate the theme of this book, it will be to your advantage to first arm yourself with knowledge so you can intelligently ask questions and make suggestions during a consolation with any professional.

WILLS

A will is a legally enforceable document effective upon the maker's (testator's death.) It declares what a person wants done with his property and often provides instructions regarding other matters.

Wills fall into three categories: noncupative or oral wills, the holographic or entirely handwritten will and the formal witnessed will which is the only type we are concerned with for our purposes. Everyone should take the trouble to have a formal will drafted. Noncupatiave and holographic wills are definitely not recommended or even recognized in some states and are useful only in unplanned emergency situations. Of course, the purpose in writing this book is to see that you never get caught in such an unplanned situation. A codicil is an amendment to an existing will and requires the same formalities as the original will.

Laws concerning the formalities of drafting wills differ form one state to another so it is wise to get local counsel. Because entire books have been written in a popular, easy-to-understand of this subject (see recommended reading list), I will only attempt to make what may seem like disjointed observations coupled with comments where I feel strongly about a particular point.

1. Women should make wills as well as men.
2. You should stay away from joint wills, that is sharing a will with your spouse.
3. Make certain you name a guardian and alternate for minor children just in case both parents die. Choose wisely and make certain you secure the proposed guardians' consent before appointing them in your will.
4. When choosing witnesses look for someone younger than you who will be easy to locate at a later date.
5. Do not let a person who is a beneficiary of the will also be a witness; while legal it is ill-advised.
6. Only very simple changes should be made by codicil. Rather than use a series of codicils to continually update the will or to institute major changes, the entire will should be rewritten.
7. Get into the habit of reviewing your will every few years to make certain you feel the same way in light of changing circumstances in your life.
8. If several different wills are offered for probate only the last will in time will be accepted.
9. Make use of the opportunity to enumerate the terms and conditions of a testamentary trust when writing your will with your attorney's assistance.
10. Decide and make it clear in the text of the will, whether each beneficiary should pay his own percentage of death taxes or whether all death taxes should be paid out of the residuary estate (what's left after specific gifts have been made.)
11. Always name an alternate or coexecutor in case the first is unwilling or unable to serve.
12. Your executor should seek the assistance of an attorney in most instances but it is to be the attorney of his choice, not yours.

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13. Personalize your will with warmth, witticism, nostalgia, etc. taking into consideration the feelings of loved ones when they hear it read at what is likely to be a psychologically painful time for them. Do not vent present anger or include anything you might possibly regret, as usually a lot of time passes between the drafting of a will and a death.

A will is a custom made document. Use it instead of letting the law determine how and to whom your assets should be distributed. The very wealthy have enough assets to take care of their loved ones no matter how poor the planning. The less property you have the more care must be taken in distributing it properly. Intestacy, as we will see next, attempts to do what the courts figure you would have wanted done if you had a say. You have that by-now- don't throw it away!

INTESTACY

It is generally believed that less than 20% of Americans have wills. Since the circumstance of your family are unique it will always be less than satisfactory to apply a standard formula when dealing with them but that is what the law must try and do when you die intestate.

The cost of drafting a will is often less than the trouble and expense of posting the bonds required by law when you die intestate. Bonds are necessary to ensure that the court appointed administrator does his job properly and to guarantee adequate performance by the guardians who must be appointed for each minor child in the absence of a will. Through your will you can also waive these bond requirements although it may not always be wise to do so.

Just how your estate will be divided varies form state to state, but a typical intestate distribution might work somewhat like this: One half of everything to your spouse, one half to children, or if more than two children then perhaps one third to spouse and two third to children or if no children, divided between spouse and parents. If you should have neither spouse, descendents nor parents living, then brothers and sisters would be next in line to inherit in most jurisdictions, followed by aunts, uncles, cousins and more distant relatives. In the rare case where no relations can be located the estate would become the property of the state. Check your state's probate code in your local library.

REASONS TO AVOID INTESTATE DISTRIBUTION

We discussed earlier, at page 280, the restrictions the law imposes on a court-appointed administrator in managing your estate which often results in an unnecessary shrinkage of assets. Not being able to choose an executor whose management abilities you trust and who could follow your instructions is one of the main disadvantages of dying intestate but even worse is not being able to control how and to whom your estate is distributed. You are prevented from using trusts for tax savings, management and to prevent certain heirs form receiving their inheritance outright with no thought as to their individual capacities to handle it.

SUMMARY

In chapter twenty-two we arbitrarily identified seven objectives of estate planning:

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1. to choose your heirs
2. cut administration costs
3. provide liquidity for the estate
4. provide financially for dependents via life insurance
5. ways to keep a business functioning or to reduce losses
6. reduce taxes
7. provide a means of transferring assets.

With proper planning we determined that:

1. assets can be transferred by the manner in which you take title to property
2. by appointing beneficiaries to receive your employment death benefits or life insurance proceeds
3. by establishing trusts during your lifetime
4. by granting powers of appointment
5. making buy-sell agreements
6. providing a lifetime giving program
7. by making a will
8. creating testamentary trust
9. by the various state laws governing intestacy.

We observed that trusts were useful for:

1. tax savings
2. providing for minors in a less rigid form than guardianship
3. affording protection from self and others
4. protecting business interests
5. granting the trustee discretion and the flexibility needed for proper management
6. allowing the assets to be managed professionally and without interruption.

We looked at the three kinds of estate: probate estate, gross estate, adjusted gross or net estate which is all that will really reach your heirs!

The worksheet should help you realize which methods you are using now and determine if some you have not yet tried could be put to good use in your particular situation.

Worksheet - Chapter Twenty-Three

WHICH METHODS OF ESTATE TRANSFER ARE YOU NOW USING OR SHOULD YOU CONSIDER

1. How do you hold title to the following:

- residence?
- vacation home?
- automobiles?
- cash and checking accounts?
- savings accounts?
- savings certificates?

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- boats?
- furs and jewelry?
- collections?
- furniture and household?
- other personal property?>
- life insurance policies?
- brokerage accounts?
- business interests?
- pension accounts?
- profit-sharing accounts?
- other retirement accounts?
- other property?
- money market funds?
- common stocks?
- mutual funds?
- corporate bonds?
- municipal bonds?
- U.S. government securities?
- U.S. savings bonds?
- preferred stocks?
- investment real estate?
- thrift plan accounts?
- credit union accounts?

2. Who is the beneficiary of your:

life insurance?
pension benefits?
all other death benefits?

3. What kinds of trusts do you have or should you consider?

- living trust
- testamentary trust
- life insurance trust
- pour-over trust
- support trust
- others
- Clifford trust
- charitable trust
- discretionary trust
- accumulation trust
- spendthrift trust

4. Have you granted or considered granting any powers-of-appointment? To whom?

5. Would a buy-sell agreement make sense in your situation?

6. Have you established an ongoing lifetime gift program?

7. Have you made a will? If not, why not? List five good reasons why you should put off making your will. List ten good reasons why you should make arrangements for drafting your will this week!

8. Check the laws governing intestacy in your state. Banks, law offices and your state bar usually have helpful pamphlets in this regard and will be glad to provide you with this information free of charge. Or check the probate code in your local law library.

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Write down in your notebook exactly how your state will distribute your assets if you die intestate. Are you completely happy with the state's arrangements or is there some way you could improve on it?

Recommended Reading
Chapters Twenty-Two and Twenty-Three

Write Your Own Will, by Robert Schwartz
Your Will and What To Do About it, by Samuel Kling
Your and Your Will, by Paul Ashley
Your Estate & Gift Taxes, by J.K. Lasser
CCH Estate Planning Guide, by Kess and Westlin
Dow-Jones Irwin Guide to Estate Planning, by William Clay, Jr.
The Complete Estate Planning Guide, by Robert Brosterman
Estate Planning After the Reagan Tax Cut, by Peter Lippett
Your Complete Guide to Estate Planning, by Parnell Callahan
How to Avoid Probate, by Norman Dacey
Personal Estate Planning, by Marcos Kinevan
The Essential of Estate Planning, by Victor Whitney
A Family Guide to Estate Planning, Funeral Arrangements and Settling an Estate After Death, by Theodore Hughes and David Klein

ADDITIONAL RECOMMENDED READING

All books written by

Sylvia Porter
Jane Bryant Quinn
Venita Van Caspel

Handbook of Investment Products & Services, by Victor Harper
Money Talks, by Bob Rosefsky
If They're So Smart, How Come You're Not Rich? by John Springer
Financial Freedom: A Positiave Strategy for Putting Your Money to Work, by Jim Barry
Economics in One Lesson, by Henry Hazlitt
The Philosophy of a Peasant, by Rodney Peterson
The Key Lecture Series: *A New Tax Structure for the United States*
The World Capital Shortage
by Bobbs-Merrill Educational Publishing
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